Riyad Capital

January 15, 2023

The Power and Water Utility Company for Jubail and Yanbu

Initiating Coverage Report

Rating	Neutral
12- Month Target Price	SAR 52.00

Price as on Jan-12, 2023	SAR 48.20
Upside to Target Price	7.9%
Expected Dividend Yield	4.6%
Expected Total Return	12.5%

Market Data

52 Week H/L	SAR 52.4/44.3
Market Capitalization	SAR 12,050 mln
Shares Outstanding	250 mln
Free Float	30%
12-Month ADTV	4,697,082
Bloomberg Code	MARAFIQ AB

Feeding KSA's Industrial Growth

Stable, dividend yielding stock

Our SAR 12.9 bln (SAR 52 per share) valuation is based on Dividend Discount Model (DDM) and relative valuations. Our key DDM assumptions include a CoE of 8.5% and a sustainable growth rate of 2.8%. Our target EV/EBITDA multiple is at 10.0x while EV/Revenues multiple is at 4.0x. MARAFIQ's future is closely tied to the industrial development in the Kingdom and to economic growth. The Company enjoys being the sole water services provider in Jubail and Yanbu industrial cities, as well as being the sole supplier of power services in Yanbu Industrial City. This makes its business more stable and in turn could pave the way for the Company to expand further into the newer cities of RIC and JCPDI, as well as participating in new competitive bids for new projects outside RC zones. We believe that the attractive dividend payout is a key investment case for MARAFIQ.

Benefitting from KSA's Industrial progress

The government's unprecedented push to spur industrial growth in the Kingdom through the established industrial cities of Jubail and Yanbu and the upcoming industrial cities of JCPDI and RIC is expected to benefit the company. MARAFIQ, is the sole energy and water provider to these cities (except power jointly through JWAP/TAWREED in Jubail).

MARAFIQ backed by impeccable shareholders

The Company is backed by some of the biggest and well know names as it counts PIF, Saudi Aramco, SABIC and Royal Commission as its four main shareholders. These shareholders are arguably the main drivers of the Saudi economy and their presence signifies the importance of MARAFIQ. These shareholders also bring key expertise to the Board of the company.

Total Revenue to grow by +4.0% CAGR between 2022-2026

Due to the steady improvement across all operating segments and nature of its utilities business, MARAFIQ has managed to deliver a stable topline over the past three years in a tight range of SAR 6.09-6.19 bln. Going forward, we believe that MARAFIQ has more room to grow in the future with a CAGR of +4.0% between 2022-2026 to reach SAR 7,528 mln in 2026.

Attractive dividend payout

Over the past three years, MARAFIQ has maintained a DPS of SAR 0.50 per share or above. The dividend policy points towards distribution of SAR 550 mln for the years 2022 and 2023. Thereafter, the payout ratio is targeted to be at 80%.

Table 1: Key Financial Figures and Ratios (2021-2025)

	2021	2022E	2023E	2024E	2025E
Income Statement (SAR mln)					
Revenues	6,192	6,450	6,716	6,987	7,252
Gross Profit	905	1,007	1,051	1,095	1,136
EBIT	998	1,137	1,187	1,237	1,284
Net Income	632	917	805	846	884
Key Ratios (%)					
Gross Margin	14.6%	15.6%	15.7%	15.7%	15.7%
EBIT Margin	16.1%	17.6%	17.7%	17.7%	17.7%
Net Margin	10.7%	14.2%	12.0%	12.1%	12.2%

Source: Riyad Capital

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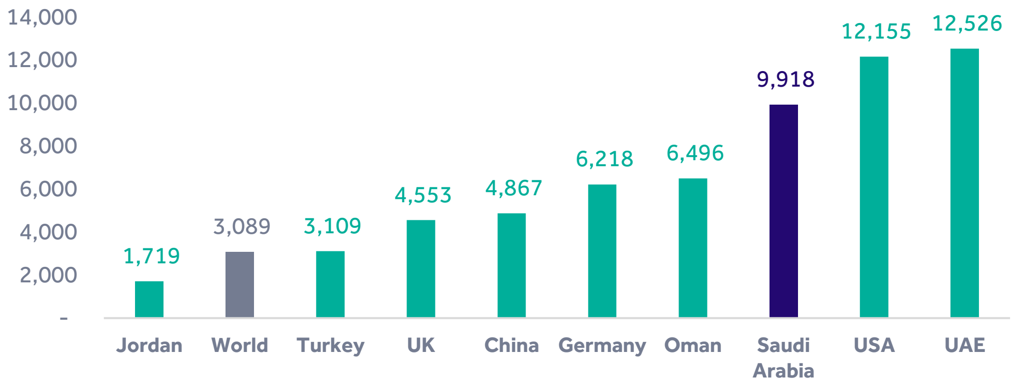
Sector Overview

Saudi Arabia has high per-capita electricity requirements

Saudi Arabia's high electricity consumption necessitates strong energy and water sectors. Electricity per-capita in 2019 was 9,918 kWh, higher than most European and MENA countries and the world average of 3,089 kWh. The higher consumption of electricity in the Kingdom is mainly due to the high residential consumption of electricity, due to the climatic considerations & social habits, increasing needs of individuals for modern electrical appliances, in addition to network losses.

Exhibit 1: Per Capita Consumption of Electricity (kWh per year)



Source: EIA, Riyad Capital

Per-capita water consumption is increasing

According to GASTAT, the Kingdom's average daily per capita water consumption increased continuously from 2010 to 2018, with a slight decrease in 2017. Per-capita water consumption in KSA was at 278 liters in 2018 as compared to Oman at 160 liters in 2019 and 127 liters in Germany. We believe the higher per-capita of water consumption in the Kingdom is due to social habits and the lack of awareness of water consumption.

Table 2: Average Daily Per Capita Consumption of Water (liters)

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Water Consumption	227	231	235	238	249	253	263	270	265	278
Growth %		1.8%	1.7%	1.3%	4.6%	1.6%	4.0%	2.7%	(1.9%)	4.9%

Source: GASTAT, Riyad Capital

Government initiatives in support of the energy sector

The government is a key contributor to the growth of numerous critical economic sectors in the Kingdom and currently owns controlling stakes in them directly or indirectly through governmental and semi-governmental bodies. However, the government intends to increase the participation of the private sector in the economy to achieve efficiency and reduce government dependence.

The objectives of Vision 2030 that are most relevant to the energy sector are to increase the contribution of renewable energy and enhance the competitiveness of the energy market. The strategy also aims to ensure sustainable use of water resources by increasing the proportion of renewable water consumption in the agricultural sector to 22.34% in 2025 from 9.49% in 2018, in addition to setting a target for renewable energy (27.3 GW by 2023). The strategy reinforces the ambition to lift untargeted energy subsidies and states that in the long term, free market prices will stimulate productivity, competitiveness among utility companies, investments and diversification of Saudi Arabia's energy mix.

Exhibit 2: Main National Transformation Programs Related to the Electricity and Water Sectors

The National Transformation Program: Improve the urban landscape and the quality of services provided in Saudi cities (utilities, public transports, etc)

National Industries Development and Logistics Services Program: Create special zones & rehabilitate economic cities, grow the contribution of renewables to the national energy mix and enhance the competitiveness of the energy sector.

Privatization Program: Grow contribution of the private sector to the economy and Unlock state-owned assets for the private sector.

Financial Sector Development Program: Enable financial institutions to support private sector growth and ensure the formation of an advanced capital market.

Source: Riyad Capital

The broad scope of the National Transformation Program is particularly relevant to the electricity sector and has led to the emergence of an ambitious program for decarbonization of power generation, which is further defined in the King Salman Renewable Energy Initiative and the National Renewable Energy Program.

Exhibit 3: The National Renewable Energy Program (NREP) Targets (GW)

Source: IRENA, Riyad Capital

Industrial Cities

MARAFIQ provides its services mainly to the two industrial cities of Jubail and Yanbu. In addition, MARAFIQ has been selected to be the provider of energy and water services to Ras Al-Khair Industrial City and Jazan City for Primary and Downstream Industries. The Royal Commission (RC) for Jubail and Yanbu is responsible for managing and supervising the development of all four industrial cities in which MARAFIQ is currently operating.

Jubail Industrial City

Jubail is located on the eastern coast of the Kingdom near to large oil fields, which makes it an ideal location for an industrial city. The city of Jubail represents over 11% of the Kingdom's non-oil GDP and accounts for about 7% of global petrochemical production. The refining capacity of Jubail is more than 0.7 mln bbl/d, making it the second largest refining center in the Kingdom after Yanbu Industrial City. In 2019, 54.7 mln tons of cargo were exported and 10 mln tons were imported through Jubail's industrial port.

Yanbu Industrial City

Yanbu was a small port city, when it was considered a suitable location for an industrial city due to its location on the Red Sea allowing access to European markets. This prompted the establishment of the third largest oil refinery center in the world with a total refinery capacity of 1.1 mln barrels (nearly a third of the Kingdom's total refinery capacity) of oil every day and yearly industrial production capacity of 131 mln tons, in addition to the largest oil shipping complex on the Red Sea (King Fahad Industrial Port).

Table 3: Number of Operating industries (2017)

	2012	2013	2014	2015	2016	2017
Operating industries	104	107	112	120	118	129
Growth %		**3%**	**5%**	**7%**	**(2%)**	**9%**

Source: MARAFIQ, Riyad Capital

As at the end of 2017, there were 129 industries operating in Yanbu Industrial City, compared to 104 in 2012, where the number of industries in Yanbu grew at an average rate of +3.6%.

Jazan City for Primary and Downstream Industries (JCPDI)

JCPDI is located on the Red Sea coast which affords it the same advantages as Yanbu City. The city also enjoys a strategic location due to its proximity to international shipping routes (Red Sea). The focus of JCPDI is towards heavy industries, petrochemical, mining and downstream industries that provide vital energy supplies, localize ship manufacturing and benefit from minerals, agriculture, wildlife and thick resources.

Ras Al Khair Industrial City (RIC)

RIC is located 60 km north of Jubail and the construction of the city and port is currently underway. The city will be devoted to processing the Kingdom's major mineral resources, phosphates and aluminum. RIC will offer a strategic link and synergies to the existing petrochemical industries in Jubail Industrial City. RIC is being developed in phases, with the aim of full completion within the next 40 years. In 2017, Aramco signed two agreements with the RC to set up two industrial projects at RIC. Currently, two industrial complexes are in operation in RIC, both of which are affiliates of the Saudi Arabian Mining Company (MAADEN): MAADEN Phosphate Company and MAADEN Aluminum Company.

Market Structure

The market structure is characterized by the presence of vertically integrated utilities, providing electricity or water services or both. In 2002, the Kingdom's government decided to increase the role of the private sector by opening the production of electricity and desalinated water to the private sector to own and operate plants and utilities in this sector.

Table 4: Summary of Electricity Generation Capacities for licensees

	Producer	No. of Plants	Capacity (MW)	% in 2021	% in 2014
Service providers	Saudi Electricity Company (SEC)	39	55,680	61.91%	71.21%
	MARAFIQ	2	2,032	2.26%	2.07%
Independent Water and Power Producers	Jubail Water & Power Company (JWAP)	1	2,876	3.20%	3.74%
	Shuaibah Water & Electricity Company (SWEC)	1	1,191	1.32%	1.55%
	Shaqaiq Water & Electricity Company (SQWEC)	1	1,020	1.13%	1.33%
Independent Power Producers	Hajr for Electricity Production Company	1	4,098	4.56%	4.44%
	Al-Mourjan for Electricity Production Company	1	2,116	2.35%	0.00%
	Durmah Electric Company (REC)	1	1,756	1.95%	2.29%
	Rabigh Electric Company	1	1,320	1.47%	1.72%
	Fadhili Plant Cogeneration Company	1	1,549	1.72%	0.00%
Other Licensees	Saline Water Conversion Corporation (SWCC)	5	9,492	10.55%	6.20%
	Saudi Aramco	9	2,279	2.53%	2.51%
	Tihama Power Generation Company	4	1,643	1.83%	1.41%
	Power Cogeneration Plant Company	3	876	0.97%	0.00%
	Rabigh Arabian Water and Electricity	1	840	0.93%	0.78%
	Others	9	792	0.88%	0.76%
Renewable Energy	Sakaka Solar Company	1	335	0.37%	0.00%
	GDFI Haradh For Energy	1	26	0.03%	0.00%
	Taqnia Energy	1	13	0.01%	0.00%
	Saudi Electricity Company (SEC)	1	3	0.00%	0.00%
	Saudi Aramco	1	3	0.00%	0.00%
Total		**85**	**89,937**	**100%**	**100%**

Source: WERA, Riyad Capital

Currently, most of the power generation in the Kingdom is concentrated through Saudi Electricity Company with 62% of generation capacity by 40 plants in 2021. However, power generation from private companies such as SWCC, ARAMCO and MARAFIQ, witnessed a continuous increase from a market share of 29% in 2014 to almost 38% in 2021, and we expect that this will continue in the future due to the privatization progress and liberalization of transmission and distribution activities.

Company Overview

MARAFIQ was founded in 2000 after a Council of Ministers Decision defined the charter of a new private utility company in mid-1999. At the beginning of 2003, it started operating commercially. The company operates, maintains, construct, and manages electric power, sea water cooling, desalinated water, and sanitary and industrial wastewater systems in all four industrial cities of the RC. Moreover, MARAFIQ is in the process of constructing and operating Sanitary Waste Water facilities in Jeddah.

The company's business is divided into three segments through the services it provides:

- **Power Segment:**

  The company provides electrical power generation, transmission, distribution and supply services in Yanbu and JCPDI.

- **Water Segment:**

  The company provides production and distribution services for desalinated and process water, potable water and industrial waste water as well as sea water cooling system and collecting & treating the sanitary wastewater in all four industrial cities.

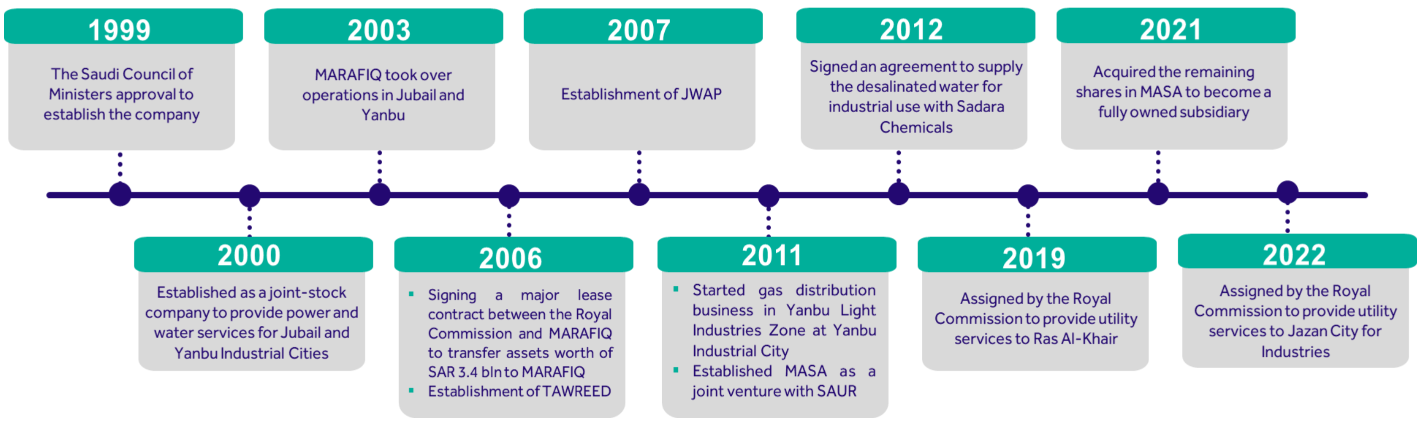
- **Sales Gas Segment:**

  The company distributes sales gas to Yanbu Light Industries Zone at Yanbu Industrial City.

MARAFIQ's Timeline

MARAFIQ has had an eventful journey since 1999. It started with the main purpose of providing essential utility services to the industrial cities of Jubail and Yanbu. Thereafter, it has expanded to reach JCPDI and RIC.

Exhibit 4: MARAFIQ's Timeline

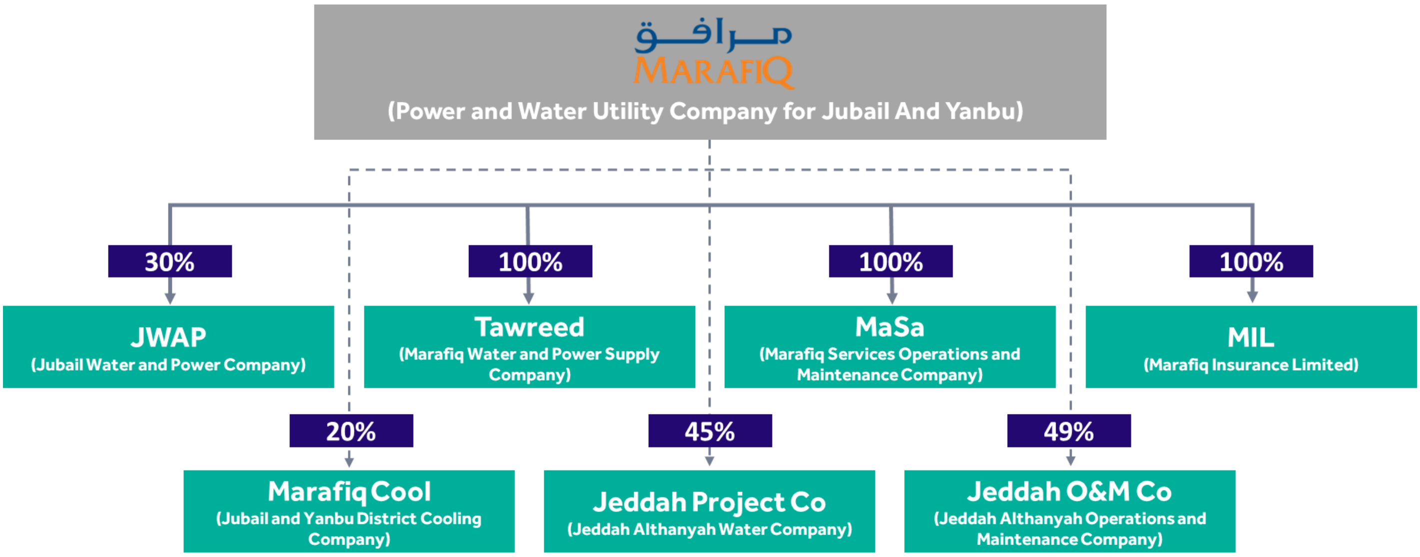


Source: MARAFIQ, Riyad Capital

Subsidiaries

MARAFIQ has the following seven subsidiaries:

Exhibit 5: Subsidiaries owned by MARAFIQ



Source: MARAFIQ, Riyad Capital

The Material Subsidiaries of the Company (subsidiaries which contribute to the equivalent of 5% or more of the Group's total assets, liabilities, revenues or income as of 2021) are JWAP, MaSa and Tawreed.

- **Jubail Water and Power Company (JWAP)**

  30% of the company is owned by MARAFIQ and it is considered as a Joint Operating Arrangement with ACWA Power and NG. JWAP is responsible to produce power and water from its cogeneration facility in Jubail city and then sells all of its power and water capacity and output to TAWREED.

- **Marafiq Water and Power Supply Co. (TAWREED):**

  Established for the purpose of purchasing water and electricity from JWAP and sell this onwards to the relevant companies. It is also responsible for the purchase of fuel from Saudi Aramco and supply of fuel to JWAP.

- **Marafiq Services Operations and Maintenance Company (MASA):**

  Established in 2011, it is responsible for the operation and management of water operation facilities in Jubail, Yanbu, JCPDI and RIC.

Shareholding Structure Pre and Post IPO

The Group's shareholders include its four founding shareholders namely; 1) Royal Commission for Jubail and Yanbu. 2) Saudi Basic Industries Corporation (SABIC). 3) Saudi Aramco Power Company (SAPCO) and 4) Public Investment Fund (PIF). There is some minor shareholding by private investors as well.

The following table details the shareholding structure Pre and Post IPO:

Table 5: Shareholding Structure Pre and Post IPO

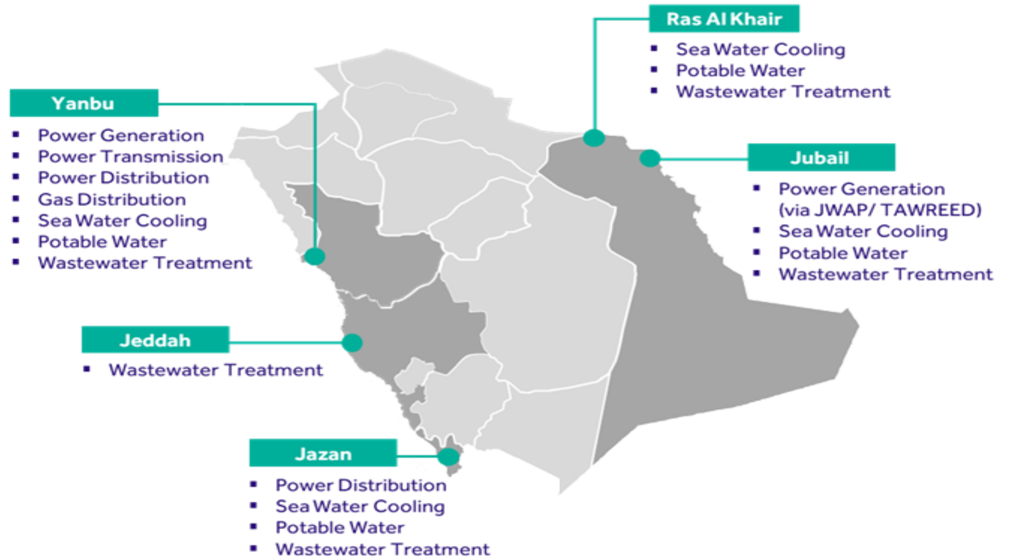
Shareholder	Pre-IPO No of Shares (mln)	Pre-IPO Ownership (%)	Post-IPO No of Shares (mln)	Post-IPO Ownership %	Ownership Change (%)
Royal Commission for Jubail And Yanbu (Royal Commission)	62,023,625	24.81%	43,750,000	17.50%	**-7.31%**
Public Investment Fund (PIF)	62,023,625	24.81%	43,750,000	17.50%	**-7.31%**
Saudi Basic Industries Corporation (SABIC)	62,023,625	24.81%	43,750,000	17.50%	**-7.31%**
Saudi Aramco Power Company (SAPCO)	62,023,625	24.81%	43,750,000	17.50%	**-7.31%**
Zamil Group Holding Co.	500,000	0.20%	500,000	0.20%	
Al Yusr Industrial Contracting Co.	200,000	0.08%	200,000	0.08%	
Khonaini International Co. LTD	1,100,000	0.44%	1,100,000	0.44%	
The National Titanium Dioxide Co. (Cristal)	100,000	0.04%	100,000	0.04%	
Rakaeez Al Jubail Holding Co.	5,500	0.002%	5,500	0.002%	
Public	-	0.00%	73,094,500	29.24%	**+29.24%**
Total	**250,000,000**	**100%**	**250,000,000**	**100%**	

Source: MARAFIQ, Riyad Capital

Geographical Locations

MARAFIQ is the sole power and water services provider for the industrial cities of Yanbu and JCPDI as well as the only water provider for the industrial cities of Jubail and RIC (whereas power jointly through JWAP/TAWREED in Jubail). The industrial cities of Jubail and Yanbu, which house several petrochemical facilities, refineries, and other complementary industrial units, are thought to be the main hubs for industrial activity in the Kingdom. In addition, the company has a presence in Jeddah city after signing an agreement with Saudi Water Partnership Company (SWPC) and Consortium to construct and operate a Sewage Treatment Plant (STP) located at Jeddah Airport in 2019. The following exhibit shows the current and planned operations in KSA.

Exhibit 6: The Current and Planned Operations of the Company in KSA



Source: MARAFIQ, Riyad Capital

It is worth noting that the Royal Commission owns all real estate within these 4 industrial cities, which means that the company leases all its assets, facilities for power, water and related lands in these cities from the Royal Commission.

Major Suppliers

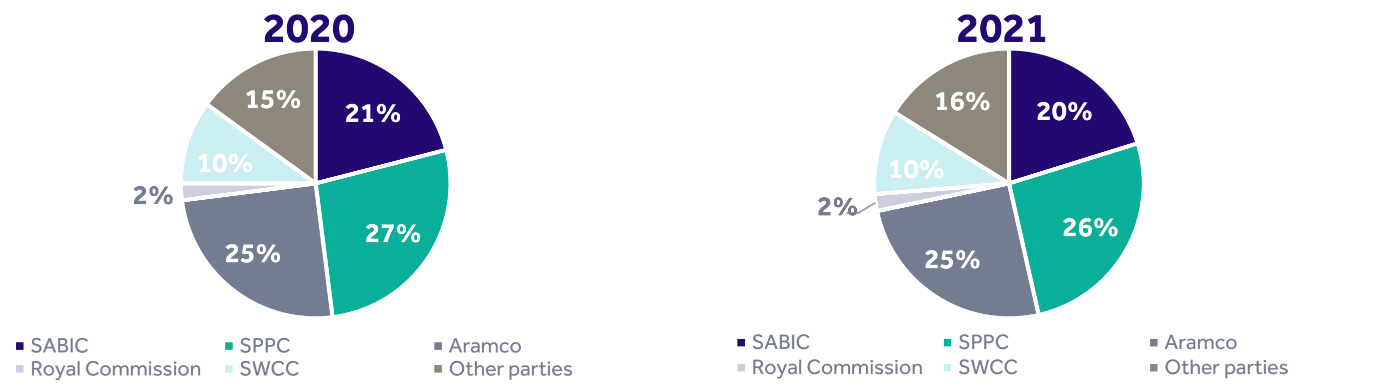
With regard to fuel, power and gas, the suppliers are a diverse number of companies, including the main shareholders of the group (such as Saudi Aramco). Saudi Aramco is considered a strategic supplier for MARAFIQ, as they provide them with the fuel which is one of the main inputs to their operations. Therefore, the company has entered into several long-term fuel agreements with Saudi Aramco, which guarantee the supply of the required fuel to the various stations of the company at prices set by the government.

Major Customers

The company's customer base consists mainly of government, commercial, residential and industrial facilities. Industrial customers represent 86% of 2021's revenue as they enjoy stable consumption levels, higher operating rates and higher tariffs compared to other customers categories. They also tend to be more prompt in making payments than the retail/household segment.

The following exhibit shows that 84% of total revenue in 2021 came from the top 5 customers namely, 1) Saudi Power Procurement Company (Principal Buyer), 2) Saudi Aramco, 3) Saudi Basic Industries Corporation (SABIC), 4) The Saline Water Conversion Corporation (SWCC) and 5) Royal Commission for Jubail and Yanbu.

Exhibit 7: Revenues Breakdown by Customer Base for 2020-2021 (%)



Source: MARAFIQ, Riyad Capital

MARAFIQ's Future Strategy

We view MARAFIQ's future as closely tied to the industrial development in the Kingdom. The Kingdom is privatizing and restructuring its power and water sectors. As part of its growth strategy, the company aims to enter into new projects outside its main organized business.

Growth within RC industrial cities

1- Organic growth:

MARAFIQ would benefit from industrial capacity expansion, mainly in Jubail and Yanbu. According to management, there are already a few requests submitted to MARAFIQ for additional power and water needs due to expansion of some of the plants. In addition, the newer cities of RIC and JCPDI offer lot of opportunities as new industries are set up which require power, water sewerage, cooling etc. infrastructure.

Organic growth can also be in the form of improving the utilization for its existing assets base. These would lead to an increase in demand for MARAFIQ's services within the current serviced clients.

2- Inorganic growth:

The company has decent cash flows to pursue inorganic growth opportunities on its own or through partnerships and Joint Ventures. These could also include revenues from long-term contracts that they are able to negotiate.

Growth across the Kingdom (outside the RC zones)

Besides operating within its core areas within the RC, the company has started exploring other opportunities. In this regard, the Company is participating in competitive bids with other parties or on an exclusive basis for new projects. An example is the Jeddah wastewater treatment plant with a total capacity of 500k m3/day that sells its entire capacity to a single off-taker (SWPC) under a 25-year PPP model.

Risks and Challenges

Capacity availability: If the company is unable to meet capacity availability guidelines due to disruption or shutdown, this would have a direct impact on the revenues and profitability. In addition, they may be subject to damages by its clients.

In 2021, power availability was at 90%, water production at 98%, sea water cooling at 94%, waste water treatment & gas was at 100%. Regular unit maintenance and servicing has ensured sufficient capacity.

Client concentration: 2021 revenues were 84% contributed from the top 5 customers. Customers include Saudi Aramco, SABIC, and RC. If one of MARAFIQ's industrial customers shuts down, reduces, or doesn't renew its agreements, it could significantly impact revenues.

The top customers also have a significant equity stake in the company and it is unlikely that they would go against the interests of MARAFIQ. In addition, Saudi Aramco, SABIC and RC are extremely strong organizations. Thus, any permanent reduction in demand or stretched shutdowns seems doubtful.

Unfavorable tariff adjustments: The majority of revenues came from water and power operations and these are mainly located in Jubail and Yanbu at present. The tariffs charged by the company for these services are set by regulatory authorities. There is a risk that this tariff is not appropriately adjusted to account for costs in the future.

Competitive Advantages

No competition in Yanbu and Jubail: MARAFIQ has a natural monopoly in water services in the industrial cities of Jubail and Yanbu (the main markets for MARAFIQ) as well as being the sole supplier of power services in Yanbu Industrial City. RC has given no rights to any other utility company in its jurisdiction to carry the water and power services. Thus, MARAFIQ currently has no competitors in these areas. In addition, RC has chosen MARAFIQ as the exclusive provider of energy and water services for RIC and JCPDI, both of which are under advanced stages of development. Thus, like Jubail and Yanbu, another competitor in these new industrial cities seems unlikely.

Large industrial customer base: MARAFIQ boasts a strong customer base which comprises mainly of large industrial clients. It is estimated that more than 80% of the company's revenues are derived from these large clients including the likes of Saudi Aramco, SABIC and the Royal Commission. Thus, the risk of default or delay in payments for services from these customers is negligible.

Impeccable shareholders: The Company is backed by some of the biggest and well know names as it counts PIF, Saudi Aramco, SABIC and Royal Commission as its four main shareholders. These shareholders are arguably the main drivers of the Saudi economy and their presence signifies the importance of MARAFIQ. These shareholders also bring key expertise to the Board of the company.

Operational Segment Analysis

Power Segment (4.8 GW Capacity)

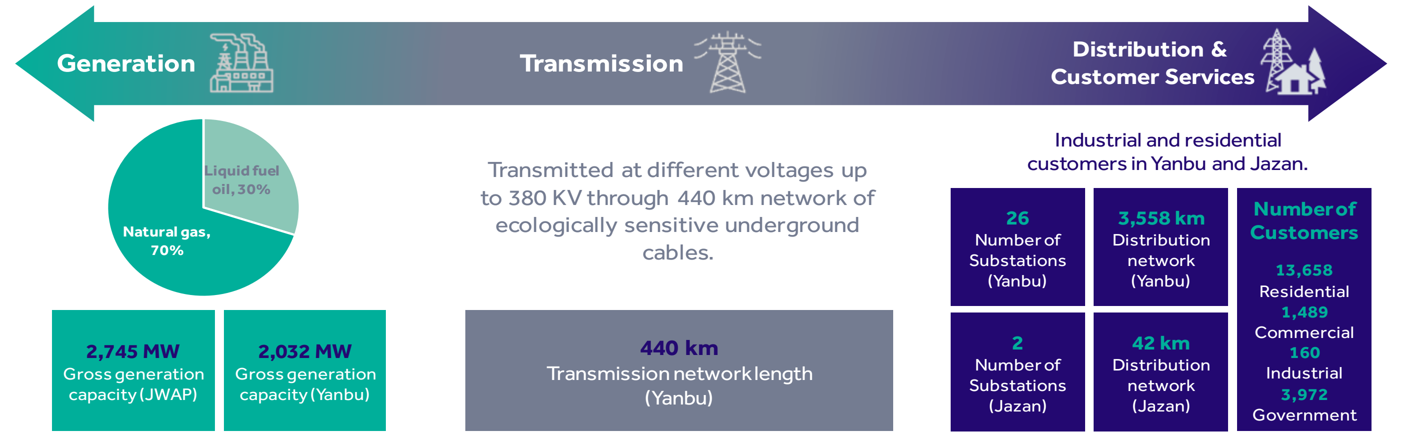
Power Segment has contributed by about 52% to MARAFIQ's 2021 total revenue.

Yanbu Industrial City: The Company generates power in Yanbu from a number of gas turbine generators (GTG) and steam turbine generators (STG). The total generation capacity of the Yanbu 1 power facilities, which consists of nine GTGs, three STGs, and three STGs from the Yanbu 2 Project, is 2,032 MW. Generating units are connected to 115kV switchyards and 380kV switchyards in Yanbu 1 and 2. In order to distribute the power generated to the industrial and community customers, many substations are well-located to serve all its customers in Yanbu industrial city. The 115kV switchyard and Yanbu 1's four major industrial substations serve most industrial customers, three community substations serve most community loads, and six satellite substations fed by major substations power selected areas. The Group expects future load growths in the Light Industrial Park (LIP) expansion and Yanbu II areas in respect of substations and transmissions. RC's development plan includes several substation and transmission projects.

Jubail Industrial City: The Company is also involved in the generation of power in Jubail industrial city through its ownership in JWAP, a 30%-owned subsidiary of the Company. JWAP through its power generation capacity of 2,745 MW, generating power and water from its cogeneration facility and then sells all of its power and water capacity to Tawreed, which in turn sells the entire power output to the Saudi Power Procurement Company (Principal Buyer) and 62.5% of the water output to Saline Water Conversion Corporation (SWCC) and 37.5% to Marafiq.

RIC & JCPDI: The Group does not conduct any power-related activities in RIC. In JCPDI, it only distributes the power it purchases in bulk from the Principal Buyer.

Exhibit 8: Fully Integrated Power Supply Chain in Yanbu With Presence in Jubail and JCPDI



Source: MARAFIQ, Riyad Capital

Water Segment

The Water Segment has contributed on average about 47% to MARAFIQ's total revenue in 2021.

Potable and Process (Treated) Water

Jubail Industrial City: Potable water in Jubail is provided mainly by JWAP. The Company has a contract for purchase of up to 300,000 m³/day of potable water from Tawreed and up to 75,000 m³/day from Al Fatah International for Water & Power Works. Moreover, a 100,000 m³/day of potable water is available from the Company's own SWRO plant in Jubail. Overall, the Company has a potable water production capacity of 1,079,000 m³/day in Jubail, including 800,000 m³/ day from the JWAP project. Furthermore, The Company has also operated the SADARA complex's Sea Water Reverse Osmosis (SWRO) plant (Kingdom's largest captive water desalination plant) for 20 years.

Yanbu Industrial City: The Company has an installed capacity of 208,240 m³/day-produces potable water mainly for residential customers, and a process water for industries. Process water is piped 51 km from power and water desalination plant storage tanks to industrial users. Meanwhile, Potable water is pumped from power and water desalination plant storage tanks to distribution tanks at two pumping stations. The total length of the potable water network is 812 km. As of last year, the average consumption of potable water was 55,000 m³/day. The treated water is stored in 23 storage tanks with a total capacity of 1,220,000 m³.

RIC: RC in the process of transferring to MARAFIQ an SWRO plant and a centralized plant for the collection and treatment of sanitary and industrial wastewater.

JCPDI: Similarly, RC is in the process of transferring to the Company certain facilities for the storage and distribution of potable and process water.

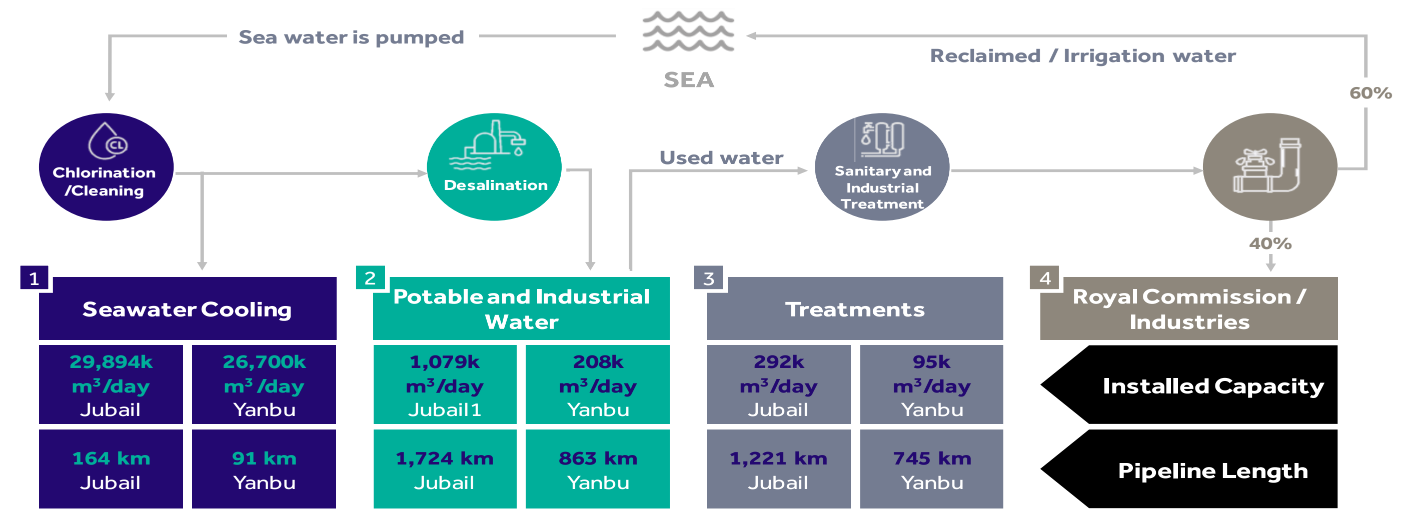
Sea Water Cooling

Due to the location of the industrial cities of Jubail and Yanbu, proximity to the coast and heavy industries, sea water is used as an external cooling system, which the company supplies to meet the needs for cooling operations. The installed capacity at Yanbu is approximately 1.1 mln m³/hour of seawater cooling and at Jubail the installed capacity is 1.2 mln m³/hour, the Jubail-2 booster pumping station has 200k m³/hour capacity and there is an additional capacity of 48k – 80k m³/hour currently under construction.

Sanitary and Industrial Waste Water

The company collects sanitary and industrial waste water (IWW) from customers in the cities of Jubail and Yanbu and this is treated in separate plants. One of the outputs of the treatment process is irrigation water, to be used mainly for irrigation purposes in these 2 cities. The installed capacity for the treatment of IWW and SWW at Jubail and Yanbu is 292,000 m³/day and 95,000 m³/day respectively. A new plant in Jubail, which is under construction, has an additional construction capacity of 120,000 m³/day for SWW and 125,000 m³/day for IWW.

Exhibit 9: Comprehensive water services in Jubail and Yanbu with growth into RCI, JCPDI and Jeddah



Source: MARAFIQ, Riyad Capital

Gas Segment (55 MMSCFD Sales Gas Capacity)

MARAFIQ's sales gas distribution business is small compared to power and water as it only represents 1% of the total revenues as of 2021. The sales gas distribution system focuses on supplying sales gas directly from large capacity pipelines to small beneficiaries in the territories that it operates in. Sales gas capacity is based on allocations from the Ministry of Energy and the allocation has increased to 55 MMSCFD to meet expected new demand. The Company procured natural gas for its sales gas distribution at a price of SAR 4.69 /MMBtu in2021.

Financial Analysis

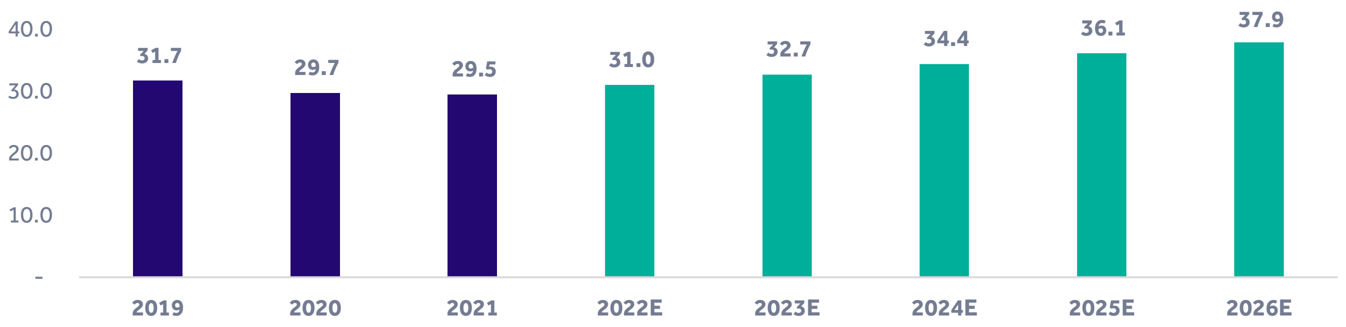
It is pertinent to note that in our financial model and analysis, we have not incorporated any tariffs changes for power, water, or gas segments. However, if approved, these tariffs changes could have a material positive impact on MARAFIQ's revenues and profitability. Our forecast is based primarily on volumes.

Growth across all operating segments

Due to its customer mix of large governmental and industrial entities with stable consumption rates, high operating rates, and higher tariffs, MARAFIQ has low volume fluctuations across its operational segments. This was further underscored during 2020 at the peak of the COVID-19 pandemic. While volumes for electricity sold dropped, this was mostly due to causes other than the pandemic. In fact, the decrease in volumes for the year 2020 was mostly due to the rehabilitation program at Yanbu, as well as, lower demand from SEC for power generated by JWAP.

We believe, the main growth drivers for MARAFIQ's power segment going forward are the increase in demand anticipated from the current clients in Jubail and Yanbu through their expansion projects as well as enhancement & optimization projects. In addition, there would be an expansion of Jazan's electrical distribution business in the future. Our assumptions call for CAGR of +5.1% for the electricity sold between 2022-2026 to reach 37.9 TWh in 2026.

Exhibit 10: Electricity Sold (TWh) Through 2026

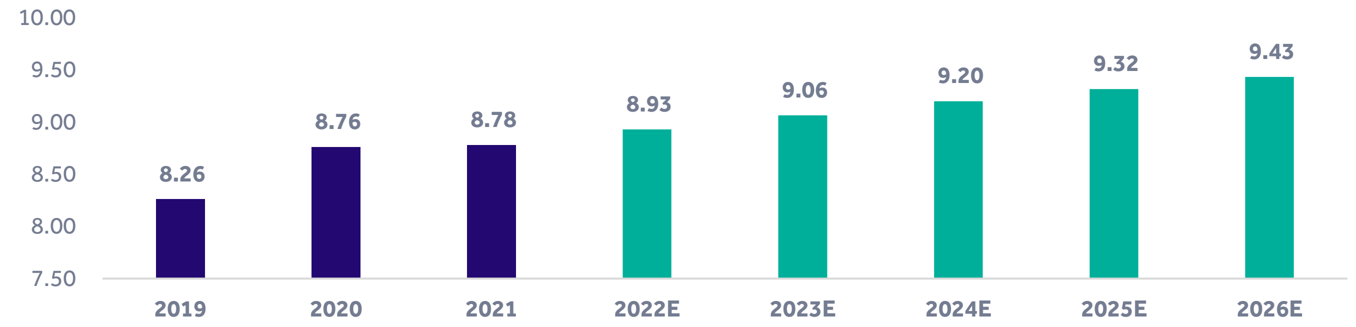


Source: MARAFIQ, Riyad Capital

Water sold continued to rise during the last three years mainly due to the Commissioning and expansion of MARAFIQ's businesses in RIC & JCPDI and the increase in Yanbu's demand for Potable and Process Water. Within the water segment, the profitability from SADARA is significantly higher than that from others. In 2021, SADARA generated SAR 263 mln (29% of total gross profit) compared to SAR 149 mln from the others, but SADARA contributed only 6.3% to revenues.

We have assumed a modest future growth in water sold with a CAGR of +1.4% between 2022-2026 to reach 9.43 bln m3 in 2026, due to some planned shut-downs. These shutdowns are likely to be offset by the water demand growth in Yanbu, RIC and JCPDI. Any inorganic growth due to projects won would be incremental to the current water volume growth forecasts.

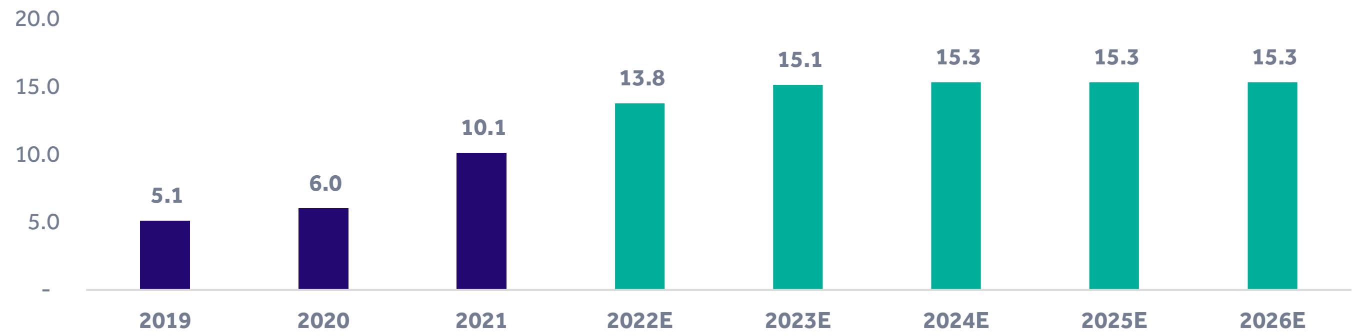
Exhibit 11: Water Sold (bln m^3) Through 2026



Source: MARAFIQ, Riyad Capital

MARAFIQ started gas distribution business in Yanbu Industrial City in 2011. During the last three years the Company witnessed an increasing growth in volumes due to expansions. Gas contributed just SAR 5 mln to total gross profits of SAR 905 mln in 2021. While we expect the momentum to continue, it is likely to be at a slower pace compared to the jump in 2021, as it reaches 15.3 MMBtu in 2024 and then to remain stable till 2026.

Exhibit 12: Sales Gas Distributed (mln MMBtu) Through 2026

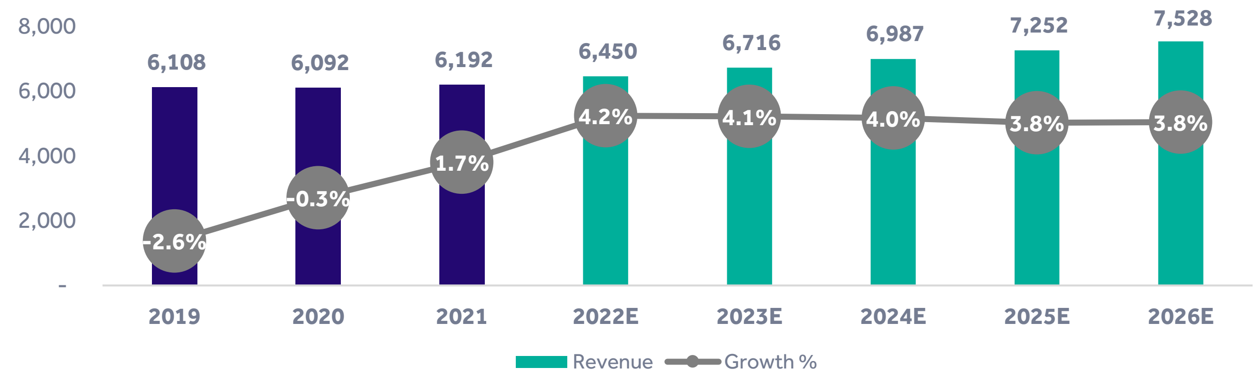


Source: MARAFIQ, Riyad Capital

Total Revenue to grow by +4.0% CAGR between 2022-2026

Due to the steady improvement across all operating segments and nature of its utilities business, MARAFIQ has managed to deliver a stable topline over the past three years in a tight range of SAR 6.09-6.19 bln. Going forward and assuming the above-mentioned growth drivers in Power, Water, and Gas volumes we believe that MARAFIQ has more room to grow in the future with a CAGR of +4.0% between 2022-2026 to reach SAR 7,528 mln in 2026.

Exhibit 13: Total Revenues Through 2026 (SAR mln)



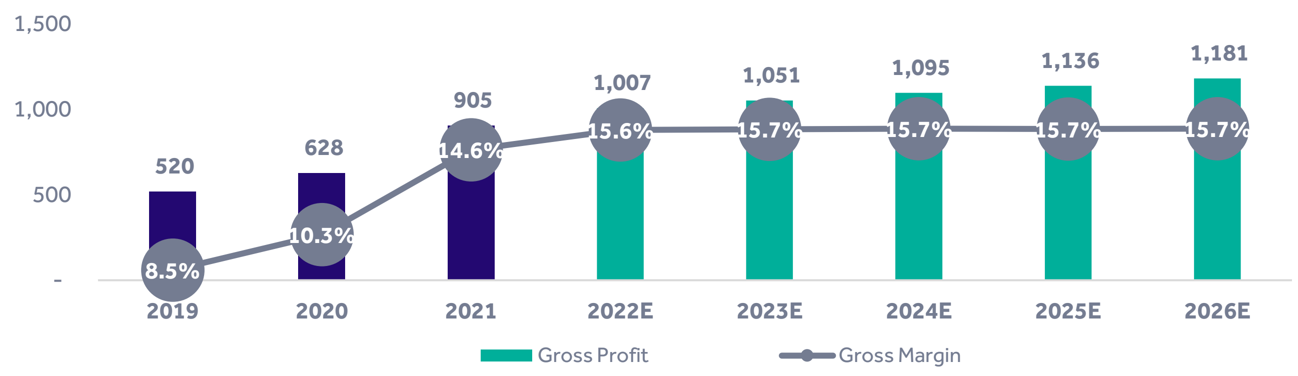
Source: MARAFIQ, Riyad Capital

Continuous improvements in gross profits

MARAFIQ's gross profit witnessed a continuous improvement during the past three years, especially in 2021, where it increased significantly by +44% Y/Y reaching SAR 905 mln. This jump occurred as the company reviewed the estimated useful life of PP&E, which resulted in a decline in depreciation expense included in the cost of revenue. It is estimated that this impact of lower depreciation was SAR 268 mln in 2021. Thus, the gross margin also increased to 14.6% in 2021, compared to 10.3% in 2020.

Going forward, we expect gross profit to grow steadily and rise to SAR 1,181 mln by 2026. In addition, we expect margins to grow to stand at 15.6% in 2022, and to stabilize thereafter.

Exhibit 14: Gross Profit and Gross Margins 2019-2026 (SAR mln)



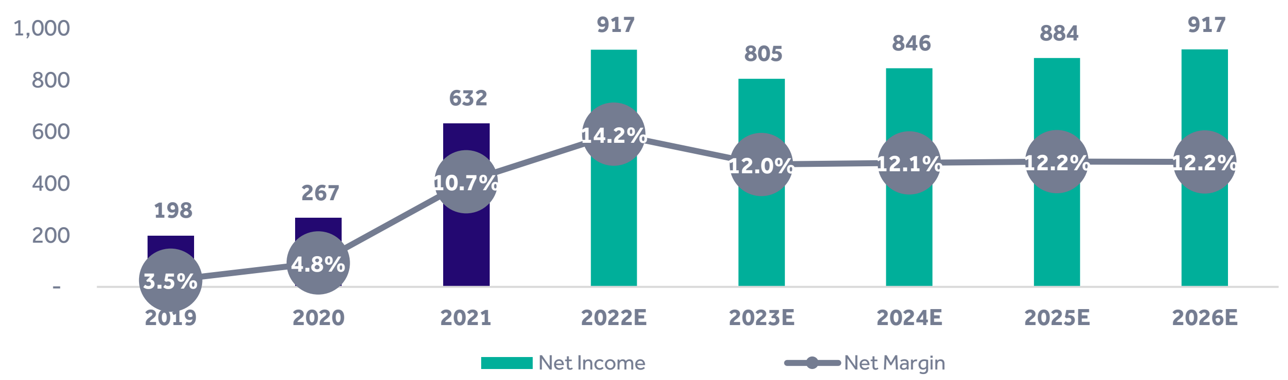
Source: MARAFIQ, Riyad Capital

Strong levels of net profit going forward

MARAFIQ has managed to generate attractive net income over the past 3 years, even in light of the ongoing expansions in JCPDI and RCI. Net income more than doubled compared to 2020, reaching SAR 632 mln in 2021. This was a result of delivering stable improvement and growth across all operating segments as well as lower depreciation expense and finance costs.

We expect the company's net income at SAR 917 mln in 2022 due to the reversal of its net deferred tax liabilities of SAR 140 mln in 4Q2022. We expect MARAFIQ's net income to increase in 2023 by +3.5% Y/Y to SAR 805 mln (without the impact of provision reversal in 2022) and subsequently rise to SAR 917 mln by 2026. Net margin is forecasted at 12.0% in 2023 rising to 12.2% by 2026.

Exhibit 15: Net Profit and Net Margins 2019-2026 (SAR mln)



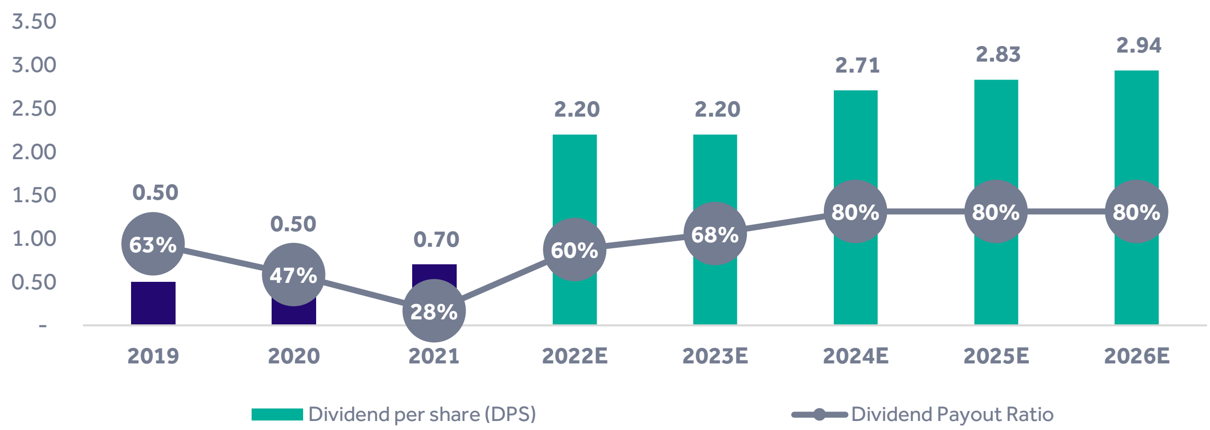
Source: MARAFIQ, Riyad Capital

Attractive dividend payout

Over the past three years, MARAFIQ has maintained a dividend per share (DPS) of SAR 0.50 per share or above, declaring total dividends of SAR 175 mln in 2021 (SAR 0.70 per share).

As per the new approved dividend policy, management expects dividend payments of SAR 550 mln for the years 2022 and 2023. Thereafter, the payout ratio is targeted to be at 80% and dividends are expected to be paid on a semi-annual basis. We believe that the attractive dividend payout is a key investment case for MARAFIQ.

Exhibit 16: Dividend per share (DPS) and Dividend Payout Ratio 2019-2026 (SAR)



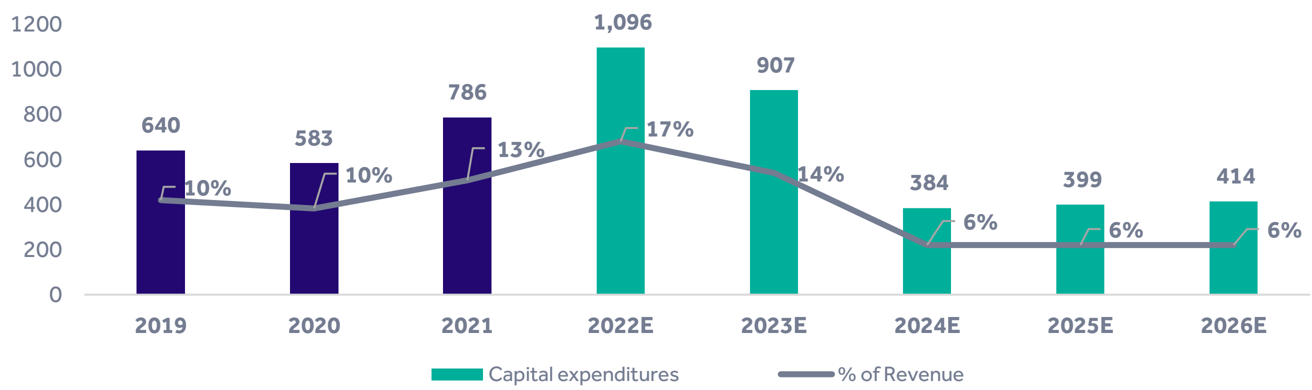
Source: MARAFIQ, Riyad Capital

Lower capital expenditure

On the back of rehabilitation of GTG (units 1 to 8) in Yanbu, installation of smart energy metering system in Yanbu and projected expansion of IWTP#8 in Jubail, we assume the capital expenditure to come in-line with the management expectation of SAR 2.0 bln between 2022-2023.

Owing to the fact that the Royal Commission develops the transmission and distribution assets in the industrial cities and transfers to MARAFIQ on a long-term financial lease, MARAFIQ is not obligated to develop power and water supply assets in the new Royal Commission industrial cities (RIC & JCPDI). Along with the management's guidance of spending a total CapEx of SAR 3.2 bln for the business plan period (2022-2026), we assume limited CapEx in the future of SAR 1.15 bln for the period between 2024-2026.

Exhibit 17: Capital Expenditures 2019-2026 (SAR mln)



Source: MARAFIQ, Riyad Capital

Net Debt to decline

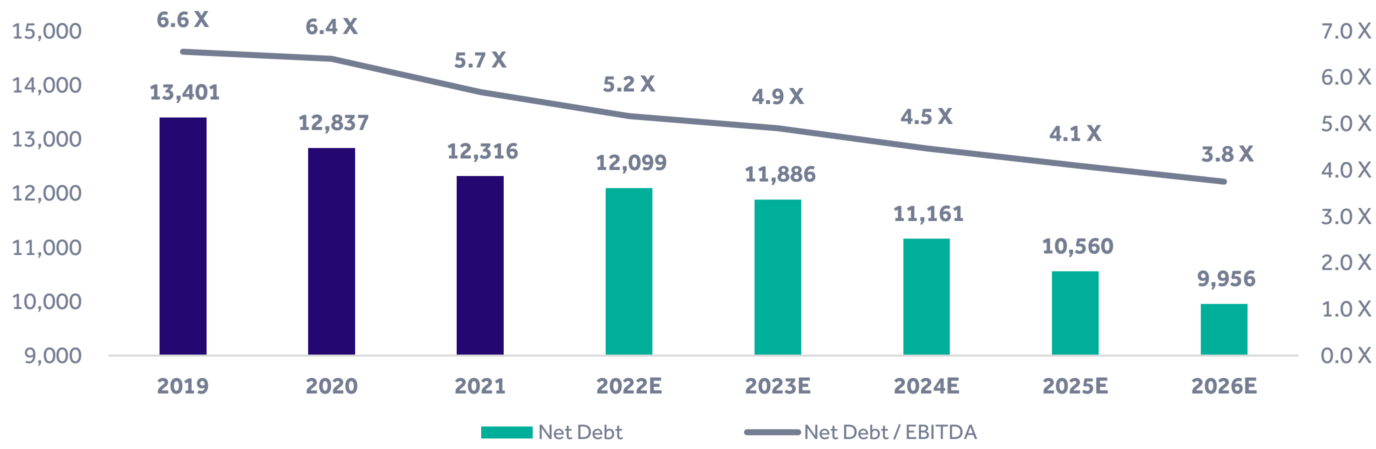
In 2016, MARAFIQ entered into a loan agreement with SIDF. This agreement calls for two SAR 1.56 bln loans to finance the construction of the Company's production facilities. During 2019, MARAFIQ signed three new loans with three banks to restructure its Murabaha facilities with longer-term loans. The additional loans, totalling SAR 6.4 bln (SAR 1.5 bln, SAR 1.5 bln, and SAR 3.4 bln), were fully utilized in 2021 and will be repaid by 2034. It is worth mentioning, MARAFIQ's Murabaha facilities of SAR 6.4 bln (as of Dec 2021) are on a floating rate basis based on SIBOR + Margin. The SIDF facilities of SAR 990 mln (as of Dec 2021) are fixed in nature offering a partial protection against interest rate fluctuations.

As for JWAP, the Company entered into three bank facilities which are partially consolidated by MARAFIQ (pro-rata 30% stake):

- **International facility:** JWAP obtained international term facility of SAR 5.90 bln to be repaid in unequal semi-annual instalments between Sep 2010 and Mar 2029. These loans have interest rates based on LIBOR plus margin.
- **Islamic facility:** structured for 20 years lease repayment with cost of the lease based on LIBOR + margin and is repayable in semi-annual instalments.
- **KEIC facility:** JWAP obtained KEIC covered loan facility of SAR 2.42 bln to be repaid in equal semi-annual instalments between Sep 2010 and Mar 2024. The facility is based on LIBOR + margin.

It is worth mentioning, JWAP facilities are hedged against interest rate fluctuations.

Exhibit 18: Net Debt / EBITDA (SAR mln)



Source: MARAFIQ, Riyad Capital
**Marafiq consolidates JWAP financials on a pro-rata ownership basis (30% stake)*
***Net debt = Bank loans and borrowings + Lease liabilities + Post-employment benefit obligations + Lease obligations for assets transferred from Royal Commission - Cash and cash equivalent*

Net debt / EBITDA for MARAFIQ gradually decreased from 6.6x in 2019 to 5.7x in 2021 due to the continuous deleveraging through repayment of certain debt facilities as well as improving EBITDA, which increased by +8.1% Y/Y in 2021. We expect Net debt / EBITDA to continue to decrease to stand at 3.8x in 2026 supported by the Company's strong ability to generate cash from operations and the Company's plans to reduce capital expenditures in the medium term in addition to the Company's plan to not raise additional debt for the period between 2022-2026.

Valuation and Financial Summery

We have valued MARAFIQ using a mixture of the Dividend Discount Model (DDM) (50%), EV/Revenue (25%) and EV/EBITDA (25%). We gave DDM a higher weight as we believe that DDM valuation method is best suited for such stocks i.e. with steady and attractive dividend payout, which is a key investment case for MARAFIQ. We arrive at a valuation of SAR 12.9 bln or SAR 51.64 per share. We initiate our coverage with a Neutral recommendation.

Valuation Summary

Valuation Method	Fair price	Weight	Weighted Average
DDM	46.25	50%	23.13
EV/EBITDA	53.06	25%	13.27
EV/Revenues	60.99	25%	15.25
Fair price (SAR)			**51.64**

1- DDM valuation at SAR 11.56 bln (SAR 46.25/share)

Using the capital asset pricing model (CAPM) to determine the cost of equity, we have used a risk-free rate of 4.5% and an equity risk premium of 4.6%. Our Beta of 0.90 is the average Beta of the following: SAUDI ELECTRICITY, AWPT, ALDREES PETROLEUM AND TRANSP and GASCO as we believe these are the four most comparable companies in the local market. We arrive at a CoE of 8.5%.

Table 6: Dividend Discount Model (DDM)

RC - Valuation	2023E	2024E	2025E	2026E
Dividends for Shareholders'	2.2	2.7	2.8	2.9
Terminal Value				**52.2**
Total Value	**2.2**	**2.7**	**2.8**	**55.1**
Discounting Factor	0.92	0.85	0.78	0.72
PV of Dividends	**2.0**	**2.3**	**2.2**	**39.7**

Terminal Perpetual Growth	2.8%
Price per share (SAR)	**46.3**

Source: Riyad Capital

Our SAR 11.56 bln (SAR46.25 per share) valuation suggests a 4.8% dividend yield. Given the current environment of high interest rates, investors might find the 4.8% yield not very appealing. However, we believe that the company has an implicit value mainly represented in its stability, shareholders who are also its main customers, and the company's ability to catch up on new opportunities that may arise from the government's plans to develop the industrial sector in the Kingdom. Thus, we incorporate this implicit value into our valuation by using the reinvested capital as an indicator for the Company's sustainable growth rate. Our 2.8% sustainable growth rate is arrived at by multiplying return on equity (ROE) by the company's retention ratio.

2- Relative Valuation at SAR 14.3 bln (SAR 57.03/share)

We have carried out a multiple based valuation as well for MARAFIQ using EV/EBITDA and EV/Revenue multiples to calculate the equity value for the Company. We have used the average multiple of eight relatively comparable companies that we have identified, which is detailed in the table below.

Table 7: Relative Valuation

EV/EBITDA Valuation			
TAQA MOROCCO	9.4x	2023E EBITDA	2,499
SAUDI ELECTRICITY CO	5.2x		
DUBAI ELECTRICITY & WATER AU	10.0x	Equity value	13,265
CHINA YANGTZE POWER CO LTD-A	11.1x	No of shares	250
CLP HOLDINGS LTD	8.7x	Fair value	53.06
NTPC LTD	8.2x		
HONG KONG & CHINA GAS	14.7x		
NATIONAL GRID PLC	12.8x		
Comparable and Target EV/EBITDA (x)	***10.0x***		

EV/Revenue Valuation			
TAQA MOROCCO	2.8x	2023E Revenue	6,716
SAUDI ELECTRICITY CO	2.8x		
DUBAI ELECTRICITY & WATER AU	5.2x	Equity value	15,247
CHINA YANGTZE POWER CO LTD-A	9.3x	No of shares	250
CLP HOLDINGS LTD	2.4x	Fair Price	60.99
NTPC LTD	2.3x		
HONG KONG & CHINA GAS	3.3x		
NATIONAL GRID PLC	4.2x		
Comparable and Target EV/Revenue (x)	***4.0x***		

Source: MARAFIQ, Riyad Capital

Table 8: Condensed Consolidated Financial Statements

Income Statement (SAR mln)	2018	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Revenues	6,271	6,108	6,092	6,192	6,450	6,716	6,987	7,252	7,528
COGS	(5,650)	(5,588)	(5,463)	(5,288)	(5,443)	(5,665)	(5,892)	(6,115)	(6,348)
Gross Profit	**621**	**520**	**628**	**905**	**1,007**	**1,051**	**1,095**	**1,136**	**1,181**
Administrative Expenses	(248)	(236)	(147)	(145)	(125)	(128)	(133)	(138)	(143)
Other items	215	433	183	238	255	264	274	285	296
Operating Profit	**587**	**716**	**664**	**998**	**1,137**	**1,187**	**1,237**	**1,284**	**1,333**
Finance Income and Cost	(330)	(505)	(292)	(217)	(251)	(272)	(279)	(287)	(294)
Zakat	(33)	3	(82)	(117)	32	(110)	(112)	(112)	(122)
Net Income	**224**	**213**	**290**	**665**	**917**	**805**	**846**	**884**	**917**
NI Attributable to Equity Holders	**204**	**198**	**267**	**632**	**917**	**805**	**846**	**884**	**917**
EBITDA	1,930	2,044	2,004	2,167	2,341	2,425	2,499	2,575	2,654
EPS	0.82	0.79	1.07	2.53	3.67	3.22	3.38	3.54	3.67
DPS	0.70	0.50	0.50	0.70	2.20	2.20	2.71	2.83	2.94

Source: MARAFIQ, Riyad Capital

Balance Sheet (SAR mln)	2018	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Assets									
Cash and ST Deposits	1,417	1,121	1,821	1,905	1,535	1,294	1,541	1,090	971
Trade Receivables	1,065	808	907	834	858	894	930	965	1,002
Others	1,414	875	795	658	666	682	696	708	718
Total Current Assets	**3,897**	**2,804**	**3,523**	**3,397**	**3,060**	**2,869**	**3,167**	**2,763**	**2,691**
PPE	20,066	20,279	20,246	20,412	20,568	20,576	20,050	19,596	19,144
Others	751	428	343	301	302	313	324	336	348
Total non-Current Assets	20,818	20,707	20,589	20,713	20,870	20,889	20,374	19,932	19,492
Total Assets	**24,714**	**23,510**	**24,112**	**24,110**	**23,930**	**23,758**	**23,542**	**22,694**	**22,183**
Liabilities & Equity									
Trade Payables	833	607	585	612	678	706	734	762	791
Others	2,687	1,585	2,035	1,584	1,625	1,623	1,667	2,356	2,093
Total Current Liabilities	**3,520**	**2,192**	**2,620**	**2,197**	**2,303**	**2,329**	**2,402**	**3,119**	**2,885**
Lease Liabilities	2,902	2,956	3,112	2,865	2,716	2,679	2,666	2,744	2,868
Others	11,452	11,484	11,392	11,497	10,892	10,476	9,968	8,149	7,564
Total non-Current Liab	14,354	14,440	14,504	14,362	13,608	13,156	12,634	10,893	10,432
Total Liabilities	**17,874**	**16,632**	**17,124**	**16,559**	**15,911**	**15,484**	**15,036**	**14,012**	**13,317**
Share Capital	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500	2,500
Retained Earnings	4,124	4,191	4,335	4,834	5,276	5,495	5,695	5,838	5,986
Statutory Reserve	240	249	261	288	313	350	382	416	451
Total Equity	6,840	6,878	6,987	7,551	8,018	8,273	8,506	8,683	8,866
Total Liab & Equity	**24,714**	**23,510**	**24,112**	**24,110**	**23,930**	**23,758**	**23,542**	**22,694**	**22,183**

Source: MARAFIQ, Riyad Capital

Cash Flows (SAR mln)	2018	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Net Income	224	213	290	665	917	805	846	884	917
Adjustments	1,886	1,999	1,804	1,555	1,443	1,639	1,675	1,714	1,762
CFO	**1,244**	**2,342**	**1,570**	**2,230**	**2,049**	**2,028**	**2,097**	**2,183**	**2,258**
Deposits	1,046	17	(1,190)	(196)	990	75	(64)	134	38
Others	(81)	(609)	(571)	(833)	(1,099)	(909)	(387)	(402)	(417)
CFI	**965**	**(592)**	**(1,761)**	**(1,029)**	**(109)**	**(835)**	**(451)**	**(268)**	**(379)**
Dividends paid	(167)	(110)	(117)	(141)	(450)	(550)	(613)	(707)	(734)
Others	(1,851)	(1,920)	(182)	(1,172)	(876)	(816)	(856)	(1,529)	(1,231)
CFF	**(2,018)**	**(2,030)**	**(299)**	**(1,313)**	**(1,326)**	**(1,366)**	**(1,469)**	**(2,236)**	**(1,965)**
Change in cash	**191**	**(279)**	**(491)**	**(112)**	**614**	**(173)**	**177**	**(322)**	**(85)**
Beginning cash	**1,173**	**1,364**	**1,085**	**595**	**483**	**1,097**	**924**	**1,101**	**779**
Cash at year end	**1,364**	**1,085**	**595**	**483**	**1,097**	**924**	**1,101**	**779**	**693**

Source: MARAFIQ, Riyad Capital

Table 9: Ratios and Key Metrics

	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Growth (YoY)								
Revenues	(2.6%)	(0.3%)	1.7%	4.2%	4.1%	4.0%	3.8%	3.8%
Power	-	(2.6%)	5.9%	5.3%	5.3%	5.3%	5.0%	5.0%
Water	-	1.8%	0.2%	1.6%	1.5%	1.5%	1.2%	1.3%
Revenue from TAWREED/JWAP	-	(1.1%)	(0.8%)	5.1%	5.8%	5.8%	5.4%	5.4%
Sales gas	-	21.2%	65.0%	36.1%	9.8%	1.3%	-	-
Gross Profit	(16.3%)	20.9%	44.0%	11.3%	4.4%	4.2%	3.8%	3.9%
Administrative Expenses	(4.5%)	(37.9%)	(1.2%)	(14.0%)	3.0%	3.5%	3.6%	3.7%
EBITDA	8.8%	(1.7%)	6.3%	3.7%	(0.5%)	(0.9%)	(0.7%)	(0.7%)
Net Income	(2.8%)	34.6%	136.8%	45.1%	(12.3%)	5.1%	4.6%	3.8%
Profitability								
Gross Margins	8.5%	10.3%	14.6%	15.6%	15.7%	15.7%	15.7%	15.7%
Adj. EBITDA Margin	33.5%	32.9%	35.0%	36.3%	36.1%	35.8%	35.5%	35.2%
Net Margins	3.5%	4.8%	10.7%	14.2%	12.0%	12.1%	12.2%	12.2%
Return on Equity	2.9%	3.8%	8.4%	11.8%	9.9%	10.1%	10.3%	10.5%
Return on Assets	0.8%	1.1%	2.6%	3.8%	3.4%	3.6%	3.9%	4.1%
Liquidity (x)								
Current Ratio	1.28	1.34	1.55	1.33	1.23	1.32	0.89	0.93
Quick ratio	1.15	1.23	1.42	1.21	1.12	1.21	0.80	0.85
Others								
EPS	0.79	1.07	2.53	3.67	3.22	3.38	3.54	3.67
DPS	0.50	0.50	0.70	2.20	2.20	2.71	2.83	2.94
Dividend Payout	63.0%	46.8%	27.7%	60.0%	68.3%	80.0%	80.0%	80.0%
Book Value per share	27.35	27.74	30.20	32.07	33.09	34.02	34.73	35.46

Source: MARAFIQ, Riyad Capital

Stock Rating

Buy	Neutral	Sell	Not Rated
Expected Total Return Greater than +15%	Expected Total Return between -15% and +15%	Expected Total Return less than -15%	Under Review/ Restricted

* The expected percentage returns are indicative, stock recommendations also incorporate relevant qualitative factors

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