3Q2023 Earnings Preview: Geopolitical Headwinds Could Overshadow Sequential Earnings Recovery

We expect 3Q2023 earnings for Qatari stocks under coverage to decline 9.2% YoY but increase 9.6% QoQ. *The YoY decline in earnings stems primarily from IQCD's skewed base effects with its profit expected to decline by almost 40%;* ***excluding Industries Qatar (IQCD), we see increases of 2.5%/5.6% YoY/QoQ in normalized aggregate earnings on the back of a moderating but strong economy with some pockets of post-World Cup momentum.*** *We note the non-oil/gas sector is recovering with PMIs starting to show a return to expansion although construction remains subdued. Meanwhile, multilateral institutions have upwardly revised global growth estimates for this year despite global macro factors tilted to the downside particularly for next year. We could see slower growth in 2024 due to an elongated global monetary tightening cycle and higher-for-longer yields than previously priced-in, a persistently weak global manufacturing sector and China's flailing real estate sector; this could be offset by continued disinflation and the rise of AI/tech. The global equity complex (ACWI) closed 3Q in the red (-3.8%; 9M2023: 8.5%) as apprehensions about "higher-rates-for-longer" took a toll.* ***Meanwhile, the QSE recovered by 1.8% in 3Q2023 (2Q2023: -1.4%; 9M2023: -4.0%),*** *while regional peers declined on average, weighed down by the Tadawul despite oil/gas prices climbing to their highest levels of the year. Overall, international foreign institutions were $40.1mn net short Qatari equities in 3Q2023 (2Q2023: $133.3mn net short) vs. $498.0mn net long in 3Q2022; as of 9M2023, foreign institutions are net short $155.9mn vs. net long of $4.4bn in 2022.*

The recent resurgence of geopolitical headwinds could ratchet up volatility, especially in the near term. Already the QSE Index is down roughly 4% in 4Q2023 vs. 3Q2023 and the upcoming earnings season could take a back seat to investor perception about heightened risk in the region. We believe that near-term market dislocations should present attractive opportunities in Qatari equites for long-term investors. *While we expect the market to remain volatile, we continue to remain positive longer-term on the Qatari market due to the following reasons:*

(1) **Favorable oil/gas supply-demand & price dynamics** on the back of sanctions by Western countries on Russia, coupled with extended oil production cuts by OPEC+ until year-end. Meanwhile, latest data show lower-than-expected stockpiles of oil in America, the lowest since July 2022 and close to operational minimums. Overall, the recent recovery in oil/gas prices to multi-month highs should lead to higher government revenue/surplus for Qatar, enabling flexibility in government spending and improving credit availability within the economy. Geopolitical concerns could also boost oil prices in the very near term.

(2) **With the successful hosting of the World Cup, perceived as one of the best editions and putting Qatar in the global spotlight, we are of the view that pockets of Qatari stock market should benefit from this success.** The ongoing Expo 2023 Doha, the Formula 1 Qatar Airways Qatar Grand Prix 2023, the MotoGP Qatar Airways Grand Prix 2023, the AFC Asian Cup Qatar 2023 and the World Aquatics Championships Doha 2024 should build on this success. Some of the impact has been immediate, with Qatar registering record visitor arrivals thus far this year.

(3) Over the medium- to long-term, **the North Field Gas Expansion, a nascent but growing tourism/sporting sector and Qatar National Vision 2030 investments** will continue to be major growth drivers for local companies.

(4) **The proposal by the QIA and GRSIA (announced in June) to restructure their local equity portfolios**, worth up to $3bn under a separate entity in a bid to increase market liquidity, is a potential tailwind for the overall stock market. Such a move could lead to a minimum of $500mn in inflows according to market estimates. Additionally, in May, the QIA committed up to QR1bn over five years to establish a permanent market-making program. This program builds on the successful initial initiative launched in September 2022, and is set to run over the next five years covering about 90% of the QSE market capitalization.

(5) On top of Qatar's macro strengths, **Qatari companies enjoy robust balance sheets backed by low leverage and decent RoEs, while Qatari banks stand out with their exceptional capital adequacy ratios, strong provision coverage and high profitability**. This should help as global monetary conditions remain tight.

Anchoring our overall convictions is that Qatari valuations are looking cheaper historically: We stay bullish longer-term on Qatari equities given their defensive characteristics backed by their strong fundamentals. The QSE's aggregate valuation metrics look attractive considering we do not see any marked medium-term earnings recession; even as the economy moderates, we note the QSE's current PE is lower than its historical median.

3rd Quarter 2023 Estimates

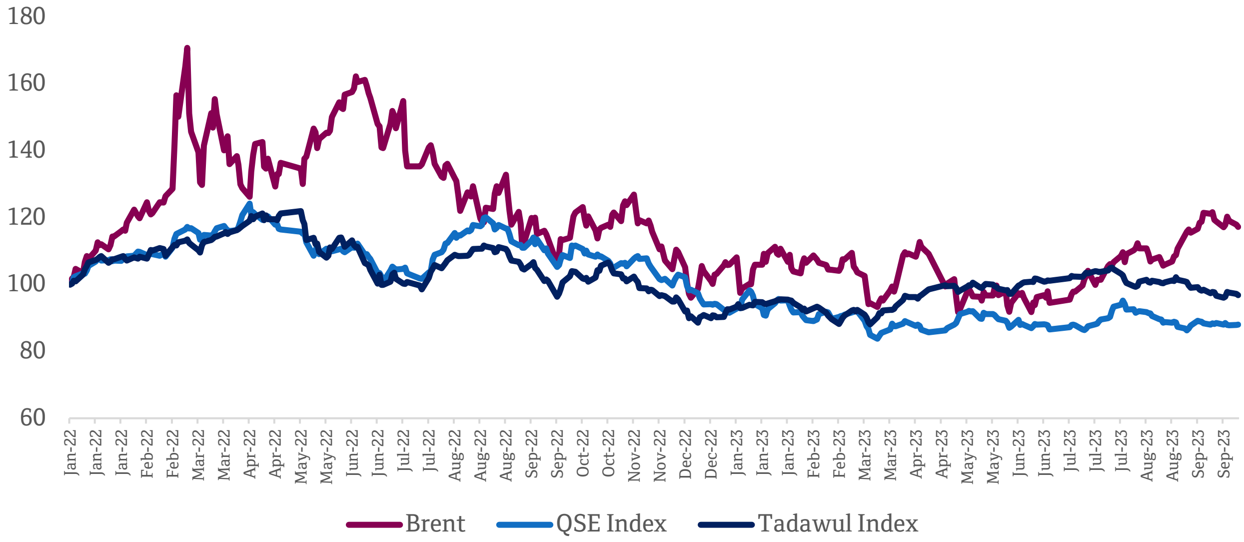
	EPS (QR)			Revenue (QR mn)		
	3Q2023e	YoY	QoQ	3Q2023e	YoY	QoQ
Ahli Bank (ABQK)	0.100	8.5%	65.2%	433.87	1.3%	18.5%
Baladna (BLDN)	0.011	165.8%	-4.3%	270.93	20.6%	3.3%
Commercial Bank of Qatar (CBQK)	0.202	6.5%	2.0%	1,501.88	9.6%	-0.4%
Doha Bank (DHBK)	0.070	-18.6%	18.9%	721.42	-2.5%	0.9%
Dukhan Bank (DUBK)	0.067	4.4%	1.0%	632.24	6.0%	11.9%
Gulf International Services (GISS)	0.076	43.1%	-26.2%	827.63	6.0%	-5.4%
Gulf Warehousing Co. (GWCS)	0.093	-8.7%	1.7%	382.47	-2.1%	2.5%
Industries Qatar (IQCD)	0.199	-38.5%	30.4%	3,173.06	-24.7%	20.4%
Estithmar Holding (IGRD)	0.023	-27.0%	-20.5%	879.10	-25.6%	22.5%
Masraf Al Rayan (MARK)	0.038	6.0%	-6.7%	941.01	-13.5%	2.7%
Qatar Electricity & Water (QEWS)	0.367	-28.5%	9.8%	740.71	4.2%	2.6%
Qatar Gas & Transport (QGTS)	0.071	-2.4%	4.4%	1,116.23	2.3%	0.3%
Qatar International Islamic Bank (QIIK)	0.232	6.2%	17.5%	477.03	0.7%	1.7%
Qatar Islamic Bank (QIBK)	0.474	8.2%	6.6%	1,658.64	5.2%	4.0%
Qatar Navigation/Milaha (QNNS)	0.270	46.4%	8.0%	746.85	-5.4%	0.3%
Vodafone Qatar (VFQS)	0.031	12.7%	5.2%	787.61	6.4%	1.6%
Medicare Group (MCGS)	0.073	-0.5%	16.9%	113.58	-0.5%	-4.5%
Total		**-9.2%**	**9.6%**	**15,404.3**	**-6.7%**	**6.5%**

Source: QNB FS Research; Note: *Revenue for GISS excludes its catering business, which is undergoing a merger

Highlights

- **We estimate banks under coverage, ex-QNB Group (QNBK) which we do not cover, to experience YoY earnings growth of 4.8%, mainly due to Qatar Islamic Bank (QIBK) and Commercial Bank of Qatar (CBQK).** The YoY aggregate performance is due to a combination of costs containment, flat to lower provisions and modest changes in margins. ***In our opinion, we do not believe 3Q results would serve as a catalyst for banks since investors would be interested in 4Q/FY2023 results and outlook on 2024. Bank stocks' performance thus far has been lackluster due to the slowdown in the domestic economy post the FIFA World Cup, along with muted credit growth. Moreover, investors are concerned with the asset quality of mid-sized banks as NPLs have spiked and Stage 2 loans have climbed with limited clarity from management on how to tackle this issue. Thus, foreign institutions have been net sellers of domestic banks. This would also explain the reason domestic banks are trading at a discount vs. regional peers.***
    - Aggregate growth in YoY earnings is attributed to **Qatar Islamic Bank (QIBK),** which continues to enjoy robust fundamentals with strong double-digit RoE generation and efficient cost management **and Commercial Bank of Qatar (CBQK),** which is modeled to benefit from investment gains (vs. losses in 3Q2022), lower CoR (1H2023: 111bps vs. FY2022: 96bps) and costs containment.
    - **QIBK is modeled to grow its net profit by 8.2% driven by some margin improvement and costs containment.** The name is trading at a 5-year low 2023e P/TB of 1.7x, which is attractive vs. its average of 2.3x and high of 3.0x.
    - **CBQK's valuation remains attractive.** The stock only trades at a P/B of 1.1x as the market is not correctly pricing in CBQK's expected strong double-digit RoE generation. The market is pricing in a sustainable RoE of 11.8% vs. our estimate of 14.8%.
    - **Sequentially, QIBK and Qatar International Islamic Bank (QIIK) are the largest contributors to aggregate earnings (we exclude Ahli Bank as the surge in its bottom-line is driven by a sharp decrease in provisions, in-line with historical trends).** QIBK is expected to follow historical trends; we pencil in healthy growth in revenue and lower provisions & impairments in 3Q2023. **QIIK's profitability is expected to be driven by a 50% decline in provisions & impairments, in-line with historical trends.** In our view, the stock is expensive as it trades at 2023e P/B of 1.9x vs. 1.7x for QIBK and 1.6x for **Dukhan Bank (DUBK).**
- **We estimate a YoY decline of 22.3% in the bottom-line of diversified non-financials under coverage mainly due to lower commodity prices and earnings decline shown by Industries Qatar (IQCD).**
    - **On a sequential basis, combined earnings of diversified non-financials could rise by 12.0% due to a rebound led by IQCD.**
    - **On a normalized basis, if we exclude IQCD from the above growth computations, earnings of non-financials should recede by only 2.4% YoY, but tick up 1.0% QoQ.**
    - **Recovery in urea prices to drive a strong sequential increase in IQCD's 3Q2023 earnings; YoY comparisons to remain moribund, however.** We expect IQCD to post a YoY net income decline of 38.5% but earnings should jump 30.4% on a QoQ basis. Urea, while still down in excess of 40% vs. yearly comparisons, is up roughly 20% sequentially in 3Q2023. Prices have strengthened as we progressed through the month of July, touching $400/MT in late July/early August and have remained strong near those levels. For reference, IQCD reported urea realizations of $531/MT in 3Q2022 and $286/MT in 2Q2023, translating into fertilizer EBITDA margins of 35% and 31%, respectively. 3Q2023 should benefit from higher realizations boosting fertilizer EBITDA margin to 37%, while fertilizer volumes should rebound QoQ post maintenance-related shutdowns in 2Q2023. On the PE front, LDPE and LLDPE prices are flattish QoQ, and down 20%/5% YoY. Steel rebar prices are marginally down QoQ (~-15% YoY) and the domestic outlook for steel demand remains constructive post a World Cup-induced lull in construction activity.
- **Risks:** Estimates can be impacted by one-offs, impairments/write-downs for non-financial companies, provisions for banks and investment income/capital gains (losses). Volatile oil & gas prices & geo-political tensions remain major risk factors to regional equities and have a direct detrimental impact on stocks under coverage.

QSE Price Performance Vs. Brent and KSA [Rebased to 100]



Source: Bloomberg, QNB FS Research

Recommendations *Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price*		Risk Ratings *Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals*	
OUTPERFORM	Greater than +20%	**R-1**	Significantly lower than average
ACCUMULATE	Between +10% to +20%	**R-2**	Lower than average
MARKET PERFORM	Between -10% to +10%	**R-3**	Medium / In-line with the average
REDUCE	Between -10% to -20%	**R-4**	Above average
UNDERPERFORM	Lower than -20%	**R-5**	Significantly above average

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