

Qatar Electricity & Water Company (QEWS)

Recommendation	OUTPERFORM	Risk Rating	R-2
Share Price	QR185.97	Current Target Price	QR223.00
Implied Upside	19.9%	Old Target Price	QR230.00

Updating Model Post 2017 Results; Stay Outperform

We maintain our Outperform rating on QEWS and continue to favor the name as a LT growth story. While 4Q2017 results were tepid and slightly confusing given the one-offs and the accounting adjustments, our LT thesis remains unchanged. We update our model with a new price target of QR223 and retain our Outperform rating on QEWS.

Highlights

- **We like QEWS as a solid long-term play with a defensive business model.** Essentially a capacity provider, QEWS takes on insignificant demand/costs/funding risks holding secure contracted assets with long-term (~25 years) fuel agreements/PWPAs and committed funding. This also leads to visible cash flows and a stable operating profile. The State of Qatar (through various entities) owns 60% of the company.
- **Market leader in Qatar with international expansion gathering steam.** Essentially a monopoly, QEWS owns stakes in all domestic IWPPs/IPPs/IWPs. Moreover, the company has diversified internationally with close to 15% of its net income expected to be driven by 60%-owned international JV (Nebras) in 2018. Nebras has operations in Indonesia, Jordan and Oman and is actively seeking opportunities in MENA and SE Asia.
- **We adjust our revenue and EBITDA downward.** Our new top-line estimates are lower by around 7%, while EBITDA estimates have been pared by 12%. Net income reduction, however, only averages around 3%. We note our model changes primarily stem from an accounting adjustment regarding RAF B. As the plant is fully depreciated, QEWS will no longer be able to record capacity charges on its top-line but will not be required to record depreciation expenses either. Some impact is also expected from a lower K-Factor at RAF A1 but this issue should be resolved by 3Q2018. [For more details, please see our alert published on February 1, 2018.](#)
- **Solid growth profile with industry leading EBITDA margins and attractive dividend/FCF yields.** 2018 will be a subdued year given expiration of RAF A in Qatar, which serves to lower EPS by 9%. Going forward, we expect EBITDA CAGR of ~2% over 2019-2023 and FCF to grow around 5% over the same period driven by Facility D (Um Al Houl) and inflation-driven capacity charge increases. Despite modeled compression, QEWS should maintain above-average EBITDA margins (average of ~48%). We expect dividend yield to average 4.5% over 2018-2023 and FCF yield to average 8.1% over the same period (despite a dip in 2018 given an expected \$250mn equity infusion into the Facility D JV). ROEs remain healthy.

Catalysts

- **New opportunities currently not in our model:** Besides Um Al Houl, our model does not account for additional expansions domestically (like Facility E; a solar project called Siraj, etc.) which will lead to LT upside. Beyond Paiton in Indonesia, we do not have color on other Nebras projects, which could lead to growth relative to our model.

Recommendation, Valuation and Risks

- **Recommendation & valuation:** *Our 12-month target is QR223.* Our new target reflects lower EBITDA estimates driven by the accounting change. The stock has shed 9% since the blockade, slightly lagging the overall market (QE Index down 8%) despite limited impact of the blockade. Shares have generated 80% in total returns over five years (DSM Index returned 27%).
- **Risks:** Geopolitical risks cannot be modeled. Besides risks inherent in international expansion, there is always a chance domestic projects get delayed or shelved. It is possible Kahramaa renegotiates the terms of existing contracts; however, this is not an imminent risk. Operational risks include availability of capacity below contracted levels, which could lead to penalties.

Key Financial Data and Estimates

	FY2017	FY2018	FY2019e	FY2020e
Revenue (QR mn)	3,071	2,493	2,637	2,697
<i>Revenue Growth</i>	<i>(1.0%)</i>	<i>(18.8%)</i>	<i>5.8%</i>	<i>2.2%</i>
EPS (QR)	14.69	13.32	14.36	14.88
<i>EPS Growth</i>	<i>4.8%</i>	<i>(9.3%)</i>	<i>7.8%</i>	<i>3.6%</i>
P/E (x)	12.7	14.0	13.0	12.5
DPS (QR)	7.75	7.75	8.00	8.25
<i>Dividend Payout</i>	<i>52.7%</i>	<i>58.2%</i>	<i>55.7%</i>	<i>55.5%</i>
<i>ROE</i>	<i>18.0%</i>	<i>15.3%</i>	<i>15.3%</i>	<i>14.8%</i>

Source: Company data, QNBFS estimates; Note: All data based on current number of shares

Key Data

Current Market Price (QR)	185.97
Current Dividend Yield (%)	4.2
Bloomberg Ticker	QEWS QD
ADR/GDR Ticker	N/A
Reuters Ticker	QEWC.QA
ISIN	QA0006929812
Sector*	Industrials
52wk High/52wk Low (QR)	232.00/161.99
3-m Average Volume ('000)	58.4
Mkt. Cap. (\$ bn/QR bn)	5.6/20.5
Shares Outstanding (mn)	110.0
FO Limit* (%)	25.0
Current FO* (%)	11.2
1-Year Total Return (%)	(13.4)
Fiscal Year End	December 31

Source: Bloomberg (as of February 11, 2018), *Qatar Exchange (as of February 11, 2018); Note: FO is foreign ownership

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Detailed Financial Statements

Income Statement (In QR mn)	FY2017	FY2018e	FY2019e	FY2020e
Revenue	3,071	2,493	2,637	2,697
Cost of Sales, Excluding Depreciation	(1,312)	(1,071)	(1,140)	(1,172)
Gross Profit	1,759	1,422	1,498	1,525
General & Administrative Expenses	(210)	(214)	(219)	(223)
EBITDA	1,549	1,207	1,279	1,302
Deferred Income	0	0	0	0
Depreciation & Amortization	(453)	(319)	(323)	(327)
EBIT	1,096	888	956	974
Finance Costs, Net	(164)	(157)	(144)	(132)
Dividend Income & Gain on Sale of AFS	95	95	79	90
Other & Miscellaneous Income/Expense & Share of Profits from JVs	613	663	713	729
Share of Associates	0	0	0	0
Profit Before Tax	1,639	1,489	1,604	1,662
Income Tax Expense	0	0	0	0
Profit After Tax (Continuing Operations)	1,639	1,489	1,604	1,662
Discontinued Operations				
Minority Interest	(23)	(24)	(24)	(25)
Profit for Shareholders	1,616	1,465	1,579	1,637
EPS (QR)	14.69	13.32	14.36	14.88

Source: Company data, QNBFS estimates

Balance Sheet (In QR mn)	FY2017	FY2018e	FY2019e	FY2020e
Non-Current Assets				
Property, Plant and Equipment	5,745	5,533	5,318	5,099
Available-for-Sale Investments	702	702	702	702
Finance Lease Receivables	1,249	1,141	1,043	954
JV Loans and Investments in JVs	3,136	4,246	4,526	4,709
Other Non-Current assets	330	322	314	306
Total Non-Current Assets	11,161	11,945	11,904	11,769
Current Assets				
Finance Lease Receivables & Others	120	120	120	120
Inventories	231	232	240	241
Accounts Receivables & Prepayments	852	854	860	864
Cash and Short-Term Deposits	3,436	2,862	3,265	3,835
Total Current Assets	4,639	4,067	4,485	5,060
Total Assets	15,800	16,012	16,388	16,829
Equity				
Equity to the Parent	8,982	9,595	10,321	11,078
Minority Interest	250	274	299	324
Total Equity	9,232	9,869	10,620	11,402
Non-Current Liabilities				
Loans and Borrowings	4,442	3,998	3,598	3,238
Employees' End of Service Benefits	74	92	111	129
Derivatives	27	27	27	27
Total Non-Current Liabilities	4,543	4,117	3,736	3,394
Current Liabilities				
Accounts Payables & Others	585	587	593	594
Loans and Borrowings	1,424	1,424	1,424	1,424
Derivatives	15	15	15	15
Total Current Liabilities	2,025	2,026	2,033	2,034
Equity and Liabilities	15,800	16,012	16,388	16,829

Source: Company data, QNBFS estimates

Recommendations

Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price

OUTPERFORM	Greater than +20%
ACCUMULATE	Between +10% to +20%
MARKET PERFORM	Between -10% to +10%
REDUCE	Between -10% to -20%
UNDERPERFORM	Lower than -20%

Risk Ratings

Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals

R-1	Significantly lower than average
R-2	Lower than average
R-3	Medium / In-line with the average
R-4	Above average
R-5	Significantly above average

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