

Qatar Electricity & Water Company (QEWS)

| Recommendation | ACCUMULATE | Risk Rating | R-2 |
|----------------|------------|----------------------|----------|
| Share Price | QR192.90 | Current Target Price | QR229.00 |
| Implied Upside | 18.7% | Old Target Price | QR215.00 |

Revising Estimates, Raising TP & Maintaining Accumulate Rating

QEWS is a low-risk play deeply linked to Qatar's growth story. We retain our long-term bullish stance on QEWS with an Accumulate rating. We also factor in a new 36 MIGD-water plant (RAF A3) from late 2016 onward and revise our estimates.

Highlights

- Growing with Qatar:** Buoyed by significant economic and population growth, Qatar's electricity & water demand is set to grow by a CAGR of 8-10% over the next few years. State-backed QEWS (43% ownership + ~11% held by Qatar Petroleum), practically Qatar's sole power & water producer, should benefit from this growth. QEWS owns 62% and 79%, respectively, of the overall power and water desalination capacity of 8,750 MW and 328 MIGD installed in Qatar.
- Watertight contracts ensure visible earnings & cash flows.** Essentially a capacity provider, QEWS buys natural gas (primary feedstock; 67% of cash direct costs, 2012-14) from QP (supplier; 100% government-owned) through long-term take-or-pay contracts and sells power and water to Kahramaa (buyer; 100%) under long-term off-take power & water purchase agreements. Fuel cost hikes are passed through to Kahramaa. These agreements lead to stable margins and any expansion should grow revenue/EPS.
- Stable operating profile and solid dividend yield should pave the way for future earnings acceleration.** Our model shows EBITDA margins remaining at industry highs of 49.3% over 2014-20. We project EPS to grow at a CAGR of 4.7% over 2014-20, despite a 0.9% decline in 2015. Dividend payout has remained a solid 53.6% over 2007-14 and we expect this trend to continue.
- Updating model and factoring in RAF 3:** We increase our 2015-16 revenue and EBITDA estimate by ~2%. Our net income forecast, however, only improves by 1% as we model in finance charges and depreciation expenses related to RAF A3.
- Seasonality should cause a sequential drop in 1Q2015.** We expect a YoY increase of 2% in revenue (-9% QoQ). Net income is projected to dip 16% QoQ but grow 2% YoY. Yearly and QoQ comparisons are also affected by the discontinuation of QEWS' satellite stations comprising roughly 2% of overall power capacity.

Catalysts

- New projects on the horizon:** QEWS should benefit from two new water plants, RAF A2 (36 MIGD) from 2H2015 and RAF A3 (36 MIGD) from 4Q2016, adding ~28% to QEWS' net water capacity. Further, Facility D (2,400 MW & 130 MIGD; 60% share) should be commissioned in 2018. We also expect contribution from Ras Laffan Industrial Water (recently upped to 65 MIGD from 36 MIGD; 60%) later in 2018. The latter two projects are not factored into our estimates/fair value. Overall, these four projects should expand QEWS' net electricity & water capacity by 27% and 73%, respectively, in 2018. QEWS is seeking regional expansion and has set up a \$1bn JV (60% stake), Nebras Power, with QPI/QH. The partners are valuing QEWS' assets in Oman & Jordan (BV: QR279.7mn) for sale to the JV; the Sur IPP in Oman is also planning an IPO in 2015.

Recommendation, Valuation and Risks

- Recommendation and valuation:** *We rate QEWS an Accumulate with a revised price target of QR229.00.* The stock trading at a 2015 P/E of 14.0x.
- Risks:** **Declining oil prices are a major risk to regional equities.** We note these further specific risks: 1) EBITDA margin erosion & 2) Foreign expansion risks.

Key Financial Data and Estimates

| | FY2013 | FY2014 | FY2015e | FY2016e |
|---------------------|--------|--------|---------|---------|
| Revenue (QR mn) | 2,904 | 2,989 | 3,116 | 3,412 |
| Revenue Growth | 2.3% | 2.9% | 4.3% | 9.5% |
| EPS (QR) | 12.58 | 13.91 | 13.79 | 14.60 |
| EPS Growth | -3.3% | 10.5% | -0.9% | 5.9% |
| P/E (x) | 15.3 | 13.9 | 14.0 | 13.2 |
| DPS (QR) | 6.82 | 7.50 | 7.75 | 8.00 |
| Dividend Payout (%) | 54.2% | 53.9% | 56.2% | 54.8% |
| Dividend Yield | 3.5% | 3.9% | 4.0% | 4.1% |
| ROE | 22.6% | 22.6% | 20.3% | 19.5% |

Source: Company data, QNBFS estimates

Key Data

| | |
|---------------------------|---------------|
| Current Market Price (QR) | 192.90 |
| Dividend Yield (%) | 4.0 |
| Bloomberg Ticker | QEWS QD |
| ADR/GDR Ticker | N/A |
| Reuters Ticker | QEWC.QA |
| ISIN | QA0006929812 |
| Sector* | Industrials |
| 52wk High/52wk Low (QR) | 208.70/162.00 |
| 3-m Average Volume ('000) | 52.2 |
| Mkt. Cap. (\$ bn/QR bn) | 5.8/21.2 |
| Shares Outstanding (mn) | 110.0 |
| FO Limit* (%) | 25.0 |
| Current FO* (%) | 10.7 |
| 1-Year Total Return (%) | 9.5 |

Fiscal Year End December 31

Source: Bloomberg (as of April 13, 2015), *Qatar Exchange (as of April 13, 2015); Note: FO is foreign ownership

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Detailed Financial Statements

| Income Statement (In QR mn) | FY2013 | FY2014 | FY2015e | FY2016e |
|--|--------------|--------------|--------------|--------------|
| Revenue | 2,904 | 2,989 | 3,116 | 3,412 |
| Cost of Sales, Excluding Depreciation | (1,148) | (1,227) | (1,321) | (1,464) |
| Gross Profit | 1,756 | 1,762 | 1,795 | 1,948 |
| General & Administrative Expenses | (215) | (225) | (226) | (247) |
| EBITDA | 1,541 | 1,537 | 1,569 | 1,701 |
| Deferred Income | 7 | 7 | 7 | 0 |
| Depreciation & Amortization | (459) | (461) | (493) | (571) |
| EBIT | 1,089 | 1,083 | 1,083 | 1,130 |
| Finance Costs | (178) | (108) | (125) | (151) |
| Interest Income, Dividend Income & Gain on Sale of AFS | 92 | 41 | 41 | 49 |
| Other & Miscellaneous Income/Expense & Share of Profits from JVs | 389 | 523 | 473 | 473 |
| Share of Associates | 19 | 28 | 80 | 144 |
| Profit Before Tax | 1,412 | 1,567 | 1,553 | 1,644 |
| Income Tax Expense | 0 | 0 | 0 | 0 |
| Profit After Tax | 1,412 | 1,567 | 1,553 | 1,644 |
| Minority Interest | (27) | (37) | (36) | (38) |
| Profit for Shareholders | 1,384 | 1,530 | 1,516 | 1,606 |
| EPS (QR) | 12.58 | 13.91 | 13.79 | 14.60 |

Source: Company data, QNBFS estimates

| Balance Sheet (In QR mn) | FY2013 | FY2014 | FY2015e | FY2016e |
|--------------------------------------|---------------|---------------|---------------|---------------|
| Non-Current Assets | | | | |
| Property, Plant and Equipment | 5,055 | 5,328 | 6,445 | 6,946 |
| Available-for-Sale Investments | 454 | 485 | 485 | 485 |
| Finance Lease Receivables | 1,775 | 1,637 | 1,523 | 1,408 |
| JV Loans and Investments in JVs | 721 | 2,567 | 2,601 | 2,635 |
| Other Non-Current assets | 267 | 424 | 432 | 453 |
| Total Non-Current Assets | 8,272 | 10,442 | 11,486 | 11,928 |
| Current Assets | | | | |
| Finance Lease Receivables & Others | 168 | 138 | 138 | 138 |
| Inventories | 276 | 195 | 210 | 233 |
| Accounts Receivables & Prepayments | 585 | 552 | 575 | 630 |
| Cash and Short-Term Deposits | 1,726 | 1,622 | 2,375 | 2,214 |
| Total Current Assets | 2,754 | 2,507 | 3,299 | 3,214 |
| Total Assets | 11,026 | 12,949 | 14,785 | 15,142 |
| Equity | | | | |
| Equity to the Parent | 6,111 | 6,782 | 7,473 | 8,226 |
| Minority Interest | 230 | 243 | 256 | 270 |
| Total Equity | 6,341 | 7,025 | 7,729 | 8,496 |
| Non-Current Liabilities | | | | |
| Loans and Borrowings | 3,361 | 3,674 | 4,763 | 4,287 |
| Deferred Income | 14 | 7 | 0 | 0 |
| Employees' End of Service Benefits | 39 | 44 | 48 | 52 |
| Total Non-Current Liabilities | 3,414 | 3,725 | 4,811 | 4,339 |
| Current Liabilities | | | | |
| Accounts Payables & Others | 689 | 603 | 649 | 711 |
| Loans and Borrowings | 413 | 1,425 | 1,425 | 1,425 |
| Derivatives | 169 | 171 | 171 | 171 |
| Total Current Liabilities | 1,272 | 2,199 | 2,245 | 2,307 |
| Equity and Liabilities | 11,026 | 12,949 | 14,785 | 15,142 |

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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