

Qatar Gas Transport Co./Nakilat (QGTS)

Recommendation	ACCUMULATE	Risk Rating	R-3
Share Price	QR17.90	Current Target Price	QR21.00
Implied Upside	17.3%		

Revising Estimates on Higher Finance Charges; Moving to Accumulate

We are lowering our earnings estimates given higher interest expenses but EBITDA forecasts remain largely the same; moving to Accumulate rating with unchanged QR21 price target. As we had discussed in our 3Q2018 results *Alert*, QGTS' third quarter 2018 operating performance was in-line with our estimates. However, softer-than-modeled JV income and higher finance expenses caused Nakilat's reported earnings to fall short of our estimates. Going forward, we are raising our interest expense forecasts and lowering our earnings estimates. Our revenue and EBITDA estimates remain largely unchanged. With the stock up around 5% since our March 13 *upgrade*, we move from an Outperform rating to an Accumulate rating with an unchanged QR21 price target. Notwithstanding some quarterly variability, QGTS' wholly-owned business remains steady and predictable. In terms of catalysts, we believe expansion of Qatar's LNG output from 77 MTPA to 110 MTPA is a significant driver (potentially another 30+ conventional vessels). Also, QGTS is targeting FSRUs with one vessel already added to the fleet. We note that the company's ships have 40-years of life vs. maximum debt life of 25 years (last debt maturing 2033), creating refinancing opportunities to increase fleet size. Medium-term, we believe the shipyard business, which is no longer loss making, could further improve.

Highlights

- **QGTS posts 8.1% YoY increase but 6.0% QoQ decline in 3Q2018 net profit missing our estimate:** Nakilat's 3Q2018 net profit of QR214.1mn fell short of our estimate of QR238.3mn (variation of -10.2%). For more details see page 2.
- **Lowering EPS estimates by 2.9% and 10.2% for 2018 and 2019, respectively; however, adjusted EBITDA up by 0.9% for 2018 and unchanged for 2019.** Our estimates have primarily been impacted by higher finance charges in 3Q2018, which we expect to continue in 4Q2018. For 2019, we expect flattish interest charges despite a 6% decline in debt given our forecast of higher interest rates.

Catalysts

- **Expansion of Qatar's LNG output from 77 MTPA to 110 MTPA is a significant driver (potentially another 30+ conventional vessels).** We continue to favor Nakilat, #1 owner/operator of LNG vessels globally, as a LT play geared to Qatari LNG's dominance and anticipated growth in the LNG market.

Recommendation, Valuation and Risks

- **Recommendation & valuation: Our 1-Year target is QR21.** QGTS trades at attractive multiples vs. peers despite higher EBITDA margins & FCF yields.
- **Risks: (1)** Blockade is an overhang but business impact has been limited thus far. Shipping ultimately remains the charterers' concern and comprehensive insurance policies (incl. war insurance) cover QGTS for political stress events under force majeure clauses for 36 months (plus 6 months in many cases). Blockage of the Strait of Hormuz/Gulf of Suez is unlikely. Charterers will also bear any costs of potential rerouting. **(2)** There is a risk existing LNG contracts get renegotiated as they are at a premium to spot (for wholly-owned fleet). We note this premium has fallen markedly over the last 12 months. Overall, we do not rule out potential contract restructuring, with QGTS accepting slightly lower charter rates in return for increasing their lengths from 25 to 35+ years. However, bargaining power rests with Qatargas and Nakilat may have no choice but to accept worse contract terms. The likelihood of this is low given investment grade-rated bonds and contagion in other GRE-related bond issues.

Key Financial Data and Estimates

	FY2016	FY2017	FY2018e	FY2019e
EPS (QR)	1.72	1.53	1.57	1.65
P/E (x)	10.4	11.7	11.4	10.8
DPS (QR)	1.00	1.00	1.05	1.10
Dividend Yield	5.6%	5.6%	5.9%	6.1%

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

Key Data

Current Market Price (QR)	17.90
Current Dividend Yield (%)	5.6
Bloomberg Ticker	QGTS QD
ADR/GDR Ticker	N/A
Reuters Ticker	QGTS.QA
ISIN	QA000A0KD6L1
Sector*	Transportation
52wk High/52wk Low (QR)	18.83/13.05
3-m Average Volume ('000)	489.8
Mkt. Cap. (\$ bn/QR bn)	2.7/9.9
EV (\$ bn/QR bn)	7.5/27.3
Shares Outstanding (mn)	554.0
FO Limit* (%)	49.0
Current FO* (%)	14.2
1-Year Total Return (%)	36.4
Fiscal Year End	December 31

Source: Bloomberg (as of November 07, 2018), *Qatar Exchange (as of November 06, 2018); Note: FO is foreign ownership

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3Q2018 Review

Higher interest charges and lower JV income lead to earnings miss. QGTS posts 8.1% YoY increase but 6.0% QoQ decline in 3Q2018 net profit missing our estimate. Nakilat's 3Q2018 net profit of QR214.1mn fell short of our estimate of QR238.3mn (variation of -10.2%).

3Q2018 Actual Vs. Estimates and Comparisons

In QR mn	3Q2018	3Q2018e	3Q2017	2Q2018	A vs. E	YoY	QoQ	2018e	2017	YoY	2016	YoY
Revenue from Wholly-Owned Vessels	774.3	777.3	770.9	768.9	-0.4%	0.5%	0.7%	3,076.9	3,057.1	0.6%	3,068.6	-0.4%
Gross Profit	596.7	600.5	593.7	593.9	-0.6%	0.5%	0.5%	2,380.8	2,359.6	0.9%	2,350.6	0.4%
EBITDA	579.4	580.0	571.5	573.0	-0.1%	1.4%	1.1%	2,307.8	2,281.4	1.2%	2,269.9	0.5%
EBIT	389.4	389.0	377.8	384.9	0.1%	3.1%	1.2%	1,551.1	1,513.4	2.5%	1,502.3	0.7%
Share of Operating Profits from Joint Ventures	101.4	113.7	91.4	106.8	-10.8%	11.0%	-5.0%	394.3	339.0	16.3%	553.4	-38.7%
Net Income to Equity	214.1	238.3	198.1	227.7	-10.2%	8.1%	-6.0%	872.3	846.2	3.1%	954.2	-11.3%
EPS (QR)	0.39	0.43	0.36	0.41	-10.2%	8.1%	-6.0%	1.57	1.53	3.1%	1.72	-11.3%
DPS (QR)								1.05	1.00	5.0%	1.00	0.0%
Adjusted Revenue	889.4	904.5	876.4	888.3	-1.7%	1.5%	0.1%	3,526.5	3,451.3	2.2%	3,677.2	-6.1%
Adjusted EBITDA	680.8	693.6	662.9	679.8	-1.8%	2.7%	0.2%	2,702.1	2,620.4	3.1%	2,823.3	-7.2%
Gross Margin	77.1%	77.2%	77.0%	77.2%				77.4%	77.2%		76.6%	
EBITDA Margin	74.8%	74.6%	74.1%	74.5%				75.0%	74.6%		74.0%	
EBIT Margin	50.3%	50.0%	49.0%	50.1%				50.4%	49.5%		49.0%	
Net Margin	27.7%	30.7%	25.7%	29.6%				28.4%	27.7%		31.1%	
Adjusted EBITDA Margin	76.5%	76.7%	75.6%	76.5%				76.6%	75.9%		76.8%	

Source: Company data, QNBFS estimates

Relative Valuation

In terms of multiples, QGTS remains relatively cheaper vs. its peers along with substantially better EBITDA margins. We also point to the company substantial FCF yield resulting from limited capex requirements and significant operating cash flow.

Relative Valuation Versus Peers

Shippers Company	Div. Ticker	Div. Yield	EBITDA Margin		P/E		P/CFPS		EV/EBITDA		FCF Yield	
			FY2018e	FY2019e	FY2018e	FY2019e	FY2018e	FY2019e	FY2018e	FY2019e	FY2018e	FY2019e
COSCO SHIPPING Energy Transportation Co Ltd	1138	1.3%	26.8%	33.5%	85.0x	14.9x	5.4x	4.1x	14.7x	10.2x	(0.3%)	4.6%
National Shipping Co of Saudi Arabia/The	NSCSA	4.5%	34.1%	NA	17.7x	13.1x	NA	NA	11.2x	NA	NA	NA
GasLog Partners LP	GLOP	8.5%	72.3%	72.4%	13.2x	11.5x	7.8x	5.9x	10.4x	9.1x	(4.1%)	0.0%
GasLog Ltd	GLOG	2.6%	69.8%	71.8%	74.1x	20.7x	8.6x	5.5x	13.1x	10.8x	(20.1%)	1.0%
Dynagas LNG Partners LP	DLNG	14.3%	72.7%	74.9%	20.2x	16.5x	6.1x	4.9x	11.2x	9.9x	NA	(95.6%)
Ship Finance International Ltd	SFL	11.0%	66.3%	74.4%	13.2x	9.7x	6.9x	6.2x	11.4x	9.1x	(23.7%)	12.3%
Teekay LNG Partners LP	TGP	3.6%	73.5%	78.2%	16.7x	7.4x	6.3x	4.4x	11.8x	9.4x	(39.2%)	(0.9%)
Golar LNG Ltd	GLNG	0.9%	52.5%	66.7%	nmf	64.2x	20.2x	12.9x	30.2x	16.1x	(2.3%)	7.9%
Tsakos Energy Navigation Ltd	TNP	5.5%	43.8%	49.7%	nmf	nmf	3.3x	2.2x	9.8x	7.6x	38.2%	44.3%
Average		5.8%	56.9%	65.2%	34.3x	19.7x	8.1x	5.8x	13.8x	10.3x	(7.4%)	(3.3%)
Median		4.5%	66.3%	72.1%	17.7x	14.0x	6.6x	5.2x	11.4x	9.6x	(4.1%)	2.8%
Qatar Gas Transport Co Ltd	QGTS	5.6%	76.6%	76.9%	11.4x	10.8x	9.3x	7.0x	10.0x	9.5x	9.8%	13.7%

Note: Where coverage is not available, estimates are based on Bloomberg consensus, if available

Mean/Median calculated if more than 3 observations are present

NA: Not Applicable

nmf: Not Meaningful (typically refers to negative or exceedingly large values)

Source: Bloomberg, QNBFS Research

Key Forecasts: Profitability and Growth Metrics

ROIC should increase over time given pay down of debt and lower interest expenses. This is despite profitability margins coming down for the 100%-owned ship fleet as we expect costs to outpace flattish top-line of wholly-owned vessels. ROE levels remain healthy.

Ratio Analysis

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030	2033
Growth Ratios (In %)												
Revenue - Wholly Owned	0.7%	(0.4%)	0.6%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%
Revenue - Adjusted	2.0%	(6.1%)	2.2%	1.2%	1.5%	(0.7%)	1.4%	1.4%	1.6%	1.4%	1.3%	1.3%
Gross Profit	0.1%	0.4%	0.9%	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)
EBITDA	(1.1%)	0.5%	1.2%	0.1%	0.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
EBITDA -Adjusted	1.1%	(7.2%)	3.1%	1.5%	1.8%	(1.0%)	1.6%	1.7%	1.9%	1.7%	1.5%	1.5%
EBIT	(6.5%)	0.7%	2.5%	0.1%	0.1%	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)	(0.0%)
EPS	(2.9%)	(11.3%)	3.1%	4.9%	13.4%	4.0%	10.5%	11.1%	11.5%	9.3%	6.0%	5.2%
CFPS	(9.9%)	16.7%	(18.5%)	33.1%	9.3%	3.2%	6.4%	7.1%	7.6%	6.4%	4.5%	4.1%
FCFPS	(4.9%)	22.0%	(26.1%)	40.5%	9.7%	3.3%	6.7%	7.4%	7.9%	6.6%	4.6%	4.2%
DPS	(20.0%)	0.0%	5.0%	4.8%	4.5%	4.3%	4.2%	4.0%	3.8%	29.6%	6.0%	5.2%
Operating Ratios (In %)												
Gross Margin	76.6%	77.2%	77.4%	77.3%	77.2%	77.1%	77.0%	76.9%	76.8%	76.7%	76.2%	75.9%
EBITDA Margin	74.0%	74.6%	75.0%	75.0%	75.0%	74.9%	74.9%	74.8%	74.8%	74.7%	74.4%	74.2%
Adj. EBITDA Margin	76.8%	75.9%	76.6%	76.9%	77.1%	76.9%	77.1%	77.3%	77.5%	77.8%	78.7%	79.2%
EBIT Margin	49.0%	49.5%	50.4%	50.4%	50.4%	50.3%	50.3%	50.2%	50.2%	50.1%	49.8%	49.6%
Net Margin	31.1%	27.7%	28.4%	29.7%	33.7%	35.0%	38.6%	42.9%	47.7%	52.2%	72.9%	85.2%
Finance Ratios												
Net Debt-to-EBITDA	8.3	7.8	7.5	7.1	6.6	6.2	5.7	5.2	4.6	4.0	0.9	-1.1
Debt-Equity Ratio	4.1	3.5	2.7	2.4	2.1	1.9	1.6	1.4	1.2	0.9	0.3	0.0
Net Debt-Equity Ratio	3.6	3.0	2.4	2.1	1.9	1.6	1.4	1.2	1.0	0.8	0.1	-0.1
Interest Coverage	1.3	1.3	1.3	1.3	1.4	1.5	1.6	1.7	2.0	2.2	5.4	36.3
EBITDA Interest Coverage	1.9	1.9	1.9	1.9	2.1	2.2	2.4	2.6	2.9	3.3	8.0	54.4
Return Ratios (In %)												
ROIC	5.6%	5.7%	5.7%	5.9%	6.1%	6.2%	6.3%	6.4%	6.5%	6.6%	7.2%	7.5%
ROAE	19.7%	15.1%	13.3%	12.3%	13.0%	12.7%	13.1%	13.5%	13.8%	13.9%	13.6%	13.2%
ROAA	3.1%	2.8%	2.9%	3.1%	3.6%	3.9%	4.4%	5.0%	5.7%	6.3%	9.9%	12.2%
Liquidity Ratios												
Current Ratio	2.0	2.0	1.7	1.5	1.5	1.4	1.4	1.4	1.3	1.3	1.2	3.7
Quick Ratio	2.0	2.0	1.6	1.5	1.5	1.4	1.4	1.4	1.3	1.3	1.2	3.7
Valuation												
EV/EBITDA-Adjusted	10.2	10.6	10.0	9.5	9.0	8.7	8.2	7.6	7.0	6.4	3.7	2.2
EV/EBIT	19.1	18.3	17.4	16.8	16.1	15.5	14.8	14.0	13.1	12.2	7.7	4.7
P/E	10.4	11.7	11.4	10.8	9.6	9.2	8.3	7.5	6.7	6.1	4.4	3.7
P/CF	8.8	7.6	9.3	7.0	6.4	6.2	5.8	5.4	5.0	4.7	3.7	3.3
P/B	1.9	1.7	1.4	1.3	1.2	1.1	1.0	1.0	0.9	0.8	0.6	0.5
Dividend Yield	5.6%	5.6%	5.9%	6.1%	6.4%	6.7%	7.0%	7.3%	7.5%	9.8%	13.7%	16.1%
FCF Yield	10.9%	13.2%	9.8%	13.7%	15.1%	15.6%	16.6%	17.8%	19.2%	20.5%	26.5%	30.1%

Source: Company data, QNBFS estimates

Detailed Financial Statements

Income Statement

Income Statement (In QR mn)	FY2017	FY2018e	FY2019e	FY2020e
Revenue – Wholly-Owned Ships	3,057	3,077	3,080	3,083
Direct Costs	(697)	(696)	(700)	(703)
Gross Profit	2,360	2,381	2,380	2,380
Income from Marine & Agency Services	55	55	56	57
General and Administrative Expenses	(133)	(128)	(126)	(125)
EBITDA	2,281	2,308	2,311	2,312
Depreciation	(768)	(757)	(757)	(758)
EBIT	1,513	1,551	1,553	1,554
Share of Profits from Joint Ventures	339	394	432	481
Finance Costs	(1,172)	(1,194)	(1,191)	(1,119)
Interest, Dividend & Profit from Islamic Banks	64	85	85	86
Vessels Sub-Chartering & Other Income	103	37	37	37
Profit Before Tax	847	873	916	1,039
Income Tax Expense	0	0	0	0
Profit After Tax	847	873	916	1,039
Minority Interest	(1)	(1)	(1)	(1)
Profit for Equity Shareholders	846	872	915	1,037
EPS (QR)	1.53	1.57	1.65	1.87
Adjusted Net Revenue	3,451	3,526	3,568	3,621
Adjusted EBITDA	2,620	2,702	2,743	2,793

Source: Company data, QNBFS estimates

Balance Sheet

Balance Sheet (In QR mn)	FY2017	FY2018e	FY2019e	FY2020e
Non-Current Assets				
Property, Plant and Equipment	22,392	21,735	21,039	20,343
Investment in Joint Venture Companies	4,144	4,502	4,632	4,752
Loans to Joint Venture Companies	99	82	82	82
Available-for-Sale Investments	109	139	139	139
Total Non-Current Assets	26,744	26,458	25,892	25,316
Current Assets				
Receivables, Inventories and Due from Joint Ventures	400	586	587	587
Cash and Bank Balances	2,775	2,590	2,342	2,169
Total Current Assets	3,175	3,176	2,929	2,757
Total Assets	29,919	29,635	28,821	28,072
Equity				
Equity Attributable to the Parent	5,922	7,210	7,674	8,232
Minority Interest	4	5	7	8
Total Equity	5,926	7,216	7,681	8,241
Non-Current Liabilities				
Borrowings	19,789	18,638	17,450	16,337
Fair Value of Interest Rate Swaps	2,478	1,738	1,614	1,490
Provision for End of Service Benefits	148	121	121	121
Total Non-Current Liabilities	22,416	20,498	19,185	17,948
Current Liabilities				
Borrowings	832	1,158	1,189	1,113
Accounts Payables/Accruals & Due to Related Parties	746	763	767	771
Total Current Liabilities	1,578	1,921	1,956	1,884
Equity and Liabilities	29,919	29,635	28,821	28,072

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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