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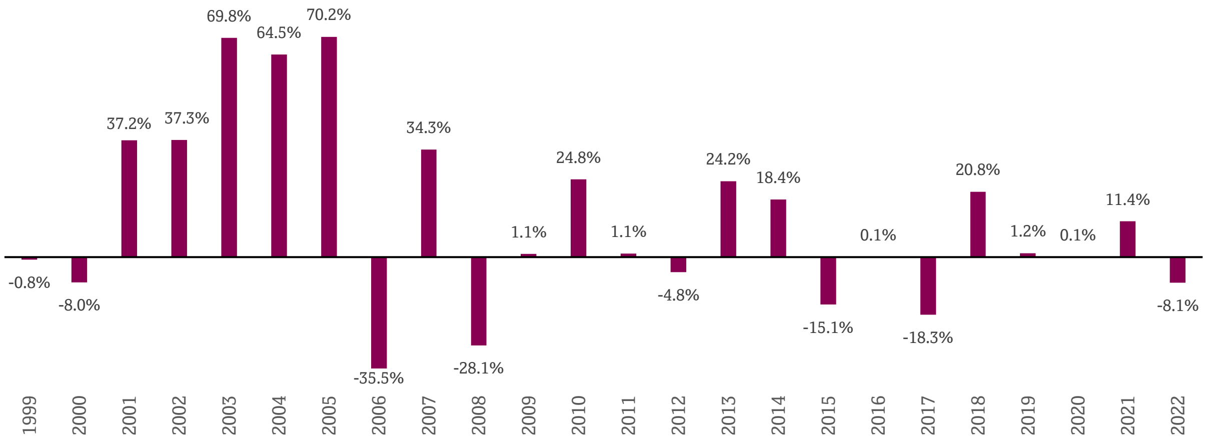
2Q2023 Earnings Preview: We Expect Flat 2Q2023 Normalized Earnings But a Strong Rebound in 2H2023

We expect 2Q2023 earnings for Qatari stocks under coverage to decline 21.4%/5.5% YoY/QoQ. *The YoY decline in earnings mostly stems from IQCD's skewed base effects with its profit expected to more than halve;* ***otherwise, we see flat earnings on the back of a moderating but strong economy, the ramping up of Qatar's massive LNG expansion project as well as some pockets of post-World Cup momentum. Overall, excluding IQCD from aggregate earnings, we expect normalized aggregate earnings for our coverage universe to edge lower by 0.8% YoY/ 3.0% QoQ.*** *Despite adversarial global macro factors – a continuation of the global monetary tightening that began early last year and weak manufacturing sector offset by a resilient labor market and the rise of AI/tech – the global equity complex (ACWI) closed the second quarter and first half of 2023 firmly in the black, up 5.6% and 12.8%, respectively, mostly driven by large-cap tech. It worth noting that, unlike at the end of the last quarter, the market and the US Fed now have converging views on the rates path as the labor markets remain resilient: The Fed Fund Futures market is pricing between 25-50bps of more rate hikes by January 2024.* ***Meanwhile, the QSE fell further by 1.4% in the second quarter (1H2023: -5.7%), while regional peers recovered somewhat, led by the Tadawul despite oil and gas prices remaining range-bound at around 18-month low levels: However, oil prices have firmed somewhat following last week's move by Opec+ to extend production cuts. Overall, international foreign institutions were $133.3mn net short Qatari equities in 2Q2023 (1Q2023: $17.5mn net long) vs. $1.3bn net long in 2Q2022. While the QSE 2Q2023 reporting season should generally be perceived positively, it is unlikely to drive near-term equity performance as the economy readjusts from elevated oil/gas prices and World Cup related activities. Global monetary conditions and recession fears should also continue to dominate sentiment.*** *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)*** *Sanctions by Western countries on Russia are still causing global oil and gas supply concerns. While the recent US banking turmoil has increased global recession fears with oil and gas prices teetering at their lows since late 2021 (although recent OPEC+ cuts will likely provide a floor), resilient consumers/labor markets and China's reopening negates some of these effects. Overall, still decent oil and gas prices should lead to higher government revenue/surplus for Qatar, enable flexibility in government expenditures and improve overall money supply (liquidity).* ***(2)*** *Furthermore, with the recent 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. 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)*** *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.* ***(5)*** *The proposal by the QIA and GRSIA (announced last month) 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, also 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, and is set to run over the next five years covering about 90% of the QSE market capitalization.* ***Qatari valuations are looking cheaper historically and 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 near-term earnings recession; even as the economy moderates, we note the QSE's current PE is lower than its historical median.* ***Moreover, from a technical viewpoint, the QSE has not experienced two consecutive down years since 2001 – it has, on average, returned 19.6% the year following a negative annual performance, though with a wide range of 0.1% to 37.2%.***

Qatar Stock Exchange Historical Price Returns



Source: Bloomberg, QNB FS Research

Highlights

- **We estimate banks under coverage, ex-QNB Group (QNBK) which we do not cover, to experience YoY earnings decline of 2.3%, mainly due to Masraf Al Rayan (MARK) as it continues to endure margin pressure. Excluding MARK, earnings are estimated to grow by 1.5%. The YoY aggregate performance is due to a combination of cost containment, flat to lower provisions and a marginal decrease/increase in margins. On the other hand, some banks are countering margin pressure with flat opex and lower CoR. Sequentially, earnings are expected to only grow by 1.4% due to Ahli Bank's (ABQK) weak QoQ performance (in-line with historical trends). Excluding ABQK, earnings are expected to move up by 3.3%.**
    - Normalized 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 Dukhan Bank (DUBK)** which is modeled to report healthy non-funded income, cost containment and book lower provisions.

  - **QIBK is modeled to grow its net profit by 3.7% driven by non-funded income, costs containment and a sharp drop in provisions** (QIBK booked large provisions in 2Q2022 and 1Q2023).
  - **Sequentially, QIBK and Commercial Bank of Qatar (CBQK) are the largest contributors to aggregate earnings.** QIBK is expected to follow historical trends; we pencil in healthy growth in revenue, lower opex and lower provisions & impairments in 2Q2023. The name is trading at a 5-year low 2023e P/TB of 1.6x, which is attractive vs. its average of 2.3x and high of 3.0x.
  - **CBQK's profitability is expected to be driven by marginal improvement in margins and cost containment.** The stock only trades at a P/TB 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 12.6% vs. our estimate of 14.8%.
- **We estimate a YoY decline of 41.9% 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 recede by 13.5% due to a largely broad-based decline led by IQCD.**
  - **On a normalized basis, if we exclude IQCD from the above growth computations, earnings of non-financials should grow 2.9% YoY and decline 12.1% QoQ.**
  - **The commodity price picture is hardly pretty, which should be reflected in IQCD's 2Q2023 results despite its diversified product profile.** We expect IQCD to post YoY and QoQ net income declines of 63.8% and 15.3%, respectively in 2Q2023. Urea continues to remain a sore spot, with prices down around 15% sequentially in 2Q2023 (down in excess of 60% YoY); prices dipped below the $300/MT level for most of the month of June as we had suspected. IQCD reported weaker-than-expected 1Q2023 results with its fertilizer EBITDA margin, driven by higher cost inventory, again retreating to their lowest level (~35%) seen in at least three years. While we believe fertilizer EBITDA margin already reached rock-bottom levels in 1Q2023 and margins should recover going forward, prices remained weaker-than-expected in 2Q2023. On the PE front, LDPE and LLDPE prices are also down roughly 10% and 5%, respectively, sequentially, and down 35%/20% YoY. Steel rebar prices are also down almost 15% QoQ (~-30% YoY) and while domestic demand is anticipated to improve post the World Cup, margins could be weak given increased sales of intermediate products much like 1Q2023. Net-net, considering that ~60% of IQCD's profitability is driven by fertilizers, we expect a weak 2Q2023 with a sequential increase in margins softening the QoQ earnings decline somewhat.
- **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.

2nd Quarter 2023 Estimates

	EPS (QR)			Revenue (QR mn)		
	2Q2023e	YoY	QoQ	2Q2023e	YoY	QoQ
Ahli Bank (ABQK)	0.059	8.3%	-26.3%	377.98	13.4%	5.6%
Commercial Bank of Qatar (CBQK)	0.192	-2.4%	3.3%	1,399.75	0.4%	-1.5%
Doha Bank (DHBK)	0.075	-11.5%	11.8%	659.00	-7.5%	3.3%
Dukhan Bank (DUBK)	0.073	6.6%	-9.0%	655.62	-3.0%	3.8%
Gulf International Services (GISS)	0.043	-5.4%	-11.4%	840.26	9.4%	0.4%
Gulf Warehousing Co. (GWCS)	0.098	1.1%	-6.3%	389.61	6.0%	-5.6%
Industries Qatar (IQCD)	0.163	-63.8%	-15.3%	2,665.08	-48.1%	-23.1%
Estithmar Holding (IGRD)	0.013	-54.8%	-55.4%	694.51	-30.9%	-9.4%
Masraf Al Rayan (MARK)	0.043	-23.0%	3.9%	912.13	-22.7%	3.6%
Qatar Electricity & Water (QEWS)	0.377	40.2%	3.5%	722.65	13.7%	9.8%
Qatar Gas & Transport (QGTS)	0.069	9.4%	-3.8%	1,067.59	0.2%	0.4%
Qatar International Islamic Bank (QIIK)	0.196	7.6%	-5.9%	486.34	12.1%	2.6%
Qatar Islamic Bank (QIBK)	0.422	3.7%	10.0%	1,567.31	-2.8%	3.5%
Qatar Navigation/Milaha (QNNS)	0.232	-6.0%	-27.4%	691.82	-19.6%	-9.7%
Vodafone Qatar (VFQS)	0.028	8.0%	-11.8%	744.20	5.5%	-4.1%
Medicare Group (MCGS)	0.054	-16.3%	-18.8%	118.06	-7.9%	-7.8%
Total		-24.1%	-5.5%	13,991.9	-17.8%	-5.4%

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

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*	
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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