# IQCD Alert – IQCD Buys 25% of QAFCO from QP; Upgrading Rating to Accumulate with QR11.50 PT

- **Industries Qatar agrees to buy remaining 25% stake in QAFCO from QP for $1bn.** In a press release, IQCD announced that its board has approved this transaction, which is now subject to shareholder approval (via an EGA) and other regulatory and customary approvals. The effective date of the Qatar Fertilizer Co. (QAFCO) transaction would be retroactive to January 1. Moreover, the board also approved a small purchase that allows QAFCO to buy QP's 40%-stake in Qatar Melamine Co. (QMC) effective July 1. **As part of the deal, QAFCO and QP have also entered into a new gas sale and purchase agreement (GSPA) covering gas requirements for QAFCO 1-6** and QMC from August 1 until December 31, 2035. Under the agreement, this 25% stake in QAFCO will revert back to QP when the above-mentioned GSPA expires in end-2035. IQCD will finance this transaction with internal cash given the company held QR11.3bn in cash/bank balances as of 1H2020.
- **Background on QAFCO and the transaction:** Established as a JV in 1969, QAFCO has become the world's largest single-site urea producer, representing ~14% share of the world's traded urea volume. Through six trains, QAFCO produces 3.8 MTPA of ammonia (~80% used for primarily urea) and 5.7-5.8 MTPA of urea. On March $8^{th}$, QP announced that it had entered into an agreement to purchase Yara's 25% stake in QAFCO for $1bn, which it now has re-sold to IQCD for $1bn. This implies similar transaction values as the QP deal – given $3.6bn in overall QAFCO net assets in 2019, this deal values QAFCO at 1.1x book value. Based on EBITDA, the deal is priced at 6.6x and 5.1x 2019 and 2018 EBITDA, respectively.
- **We expect favorable financial impact on IQCD from two sources: (1) extra 25% contribution from QAFCO and (2) favorable blended gas price for new GSPA for QAFCO 1-6.** We remind investors that the prior GSPA, which set the feedstock price for trains 1-4, expired in December 2019 and was replaced on an interim basis by a gas processing agreement. IQCD, in its press release, states that this deal will provide a positive NPV with a buoyant IRR. We believe this new GSPA will lower the overall blended gas price for QAFCO 1-6 vs. the previous blended gas cost (that involved a higher price for the older QAFCO 1-4 trains along with more attractive gas feedstock cost for QAFCO 5-6). *Continued on page 2.*

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- **We see modest upside to our existing QR1.4bn earnings estimate for IQCD in 2020.** 100% consolidation of QAFCO would add QR93mn or 19% to IQCD's reported 1H2020 net income of QR485mn, bringing it up to QR578mn. Looking at it on a segment level, QAFCO at 100%, added QR371mn in 1H2020 net income, which is around 45% of our 2020 net income estimate for QAFCO. Given our expectation of a 2H recovery and IQCD's comments of favorable new gas pricing, we could end up with a modest upside to our overall 2020 net income forecast for IQCD of QR1.4bn. We await more details from management and could change our estimates going forward.
- **Could acquisitions of the remaining stakes of 20% in QAPCO and 50% in QAFAC, respectively, provide further catalysts for stock price upside?** We could witness similar deals concerning these JVs, especially in light of QP's strong deal-making ability and bargaining power relative to minority partners and IQCD's robust cash position/cash generating ability. **Indeed an agenda item in the upcoming EGA, which authorizes IQCD's board (controlled by Special Shareholder QP) to negotiate transactions with JV partners, could pave the way for similar deals in the future.**
- **We upgrade IQCD from Market Perform to Accumulate with a QR11.50 price target.** Our previous price target was QR10. Although recent strong stock price activity suggests that this deal could be somewhat baked into the current price, valuing QAFCO at 100% in our DCF model allows us to up our price target. We will fine tune our model when more details become available.



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| Recommendations<br>*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<br>*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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