

Qatar Electricity & Water Company (QEWS)

Recommendation	ACCUMULATE	Risk Rating	R-2
Share Price	QR160.98	Current Target Price	QR184.00
Implied Upside	14.3%	Old Target Price	QR204.00

Lowering Estimates & Price Target; Maintain Accumulate

We are lowering our estimates and target price for QEWS given weaker-than-expected 1Q2019 results and lower tariff/offtake forecasts. 1Q2019 results were soft with seasonal weakness exacerbated by tariff/offtake impact from RAF B, RAF B1 and RAF B2. Potential tariff revisions have always been a substantial risk to QEWS and we see some of this playing out over the upcoming quarters. Admittedly our revised forecasts could be too low especially when it comes to Nebras but we chose to adopt a conservative view. We continue to like the company as a long-term play with a relatively defensive business model. QEWS still enjoys decent EBITDA margins and dividend/FCF yields. LT catalysts (which we have not yet factored into our estimates) abound, including additional expansions domestically (like Facility E; the Siraj solar project, etc.). Beyond Paiton (Indonesia), we do not have color on other Nebras projects, which could lead to growth relative to our model. As a result of our model changes, we lower our price target from QR204 to QR184; in light of the stock's decline, we maintain our Accumulate rating.

Highlights

- What's changed? – Revenue/tariff pressure evident with weak 1Q2019 results.** RAF B, which already witnessed lowered tariffs under a 12-year contract extension from July 2018, also faces lower offtake this year given Umm Al Houf (which is running at full capacity). Moreover, RAF B1/B2 are going through a contractually agreed dip in tariff rates this year.
- QNB FS forecasts: 2019 revenue/EPS decreases from QR2.6bn/QR13.95 to QR2.3bn/QR11.73 and 2020 revenue/EPS goes from QR2.6bn/QR14.37 to QR2.3bn/QR12.07.** The aforementioned changes in tariffs/offtakes came as a surprise and we have adjusted our model accordingly. Our forward revenue/EPS estimates decrease by an average of 12%/16%. Our forward EBITDA estimates have also come down by 15%. We have also kept our DPS flat at QR7.75 over our forecast period vs. our previous estimate of modest growth from 2021 onward. For more details regarding our new estimates, please see page 2.
- Despite our lowered forecasts, QEWS still enjoys decent EBITDA margins and dividend/FCF yields.** Despite modeled compression, QEWS should still maintain decent EBITDA margins (2019-2023 avg.: ~44%). Over 2018-2023, we expect dividend yield to average 4.8% and FCF yield to average 7.3% (despite a dip in 2018 as QEWS invested \$252mn into the Facility D JV). ROEs average around 12.0% over 2019-2023.

Catalysts

- New opportunities currently not in our model:** Besides Umm Al Houf (Facility D), our model does not account for additional JV expansions domestically (like Facility E; a solar project called Siraj, etc.) which will lead to LT upside. **Facility E, which is Umm Al Houf's size** (power: 2,000–2,500 MW & water: 100-130 MIGD), should be commissioned before summer 2022. Siraj should start production in late 2020 with 350 MW with possible expansion to 900 MW subsequently. Beyond Paiton in Indonesia, we do not have color on other Nebras projects, which could lead to growth relative to our model. Ultimately, our JV income forecasts could prove to be conservative – we are expecting 11.4% growth from QR542mn in 2018 to QR604mn in 2019 and a 2.7% CAGR over 2019-2023.

Recommendation, Valuation and Risks

- Recommendation & valuation:** Our 1-year PT is QR184. 2019 & 2020 P/Es seem rich at 13.7x and 13.3x, respectively.
- Risks: Geopolitical risks** cannot be modeled. Besides risks in international expansion, there is always a chance domestic projects get delayed/shelved. It is possible Kahramaa substantially renegotiates the terms of existing contracts and recent discussions on K-Factors gives us pause. We note the July 2018 lower-than-expected rates for RAF B involve a contract extension on a fully-depreciated plant. However, contract terms are proprietary and we cannot rule out further unanticipated declines in tariffs/offtake terms as witnessed in 1Q2019. **Operational risks include availability of capacity below contracted levels**, which could lead to penalties.

Key Financial Data and Estimates

	FY2018	FY2019e	FY2020e	FY2021e
Revenue (QR mn)	2,601	2,257	2,299	2,344
Revenue Growth	-15.3%	-13.2%	1.9%	1.9%
EPS (QR)	13.97	11.73	12.07	12.75
EPS Growth	-4.9%	-16.0%	2.9%	5.7%
P/E (x)	11.5	13.7	13.3	12.6
DPS (QR)	7.75	7.75	7.75	7.75
ROE	14.7%	12.3%	12.1%	12.1%

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

Key Data

Current Market Price (QR)	160.98
Current Dividend Yield (%)	4.8
Bloomberg Ticker	QEWS QD
ADR/GDR Ticker	N/A
Reuters Ticker	QEWC.QA
ISIN	QA0006929812
Sector*	Industrials
52wk High/52wk Low (QR)	200.00/160.00
3-m Average Volume ('000)	29.2
Mkt. Cap. (\$ bn/QR bn)	4.9/17.7
EV (\$ bn/QR bn)	5.8/21.2
Shares Outstanding (mn)	110.0
FO Limit* (%)	49.0
Current FO* (%)	12.6
1-Year Total Return (%)	(14.1)
Fiscal Year End	December 31

Source: Bloomberg (as of March 23, 2019), *Qatar Exchange (as of March 22, 2019); Note: FO is foreign ownership

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Summary of Estimate Changes

QNB FS forecasts: 2019 revenue/EPS decreases from QR2.6bn/QR13.95 to QR2.3bn/QR11.73 and 2020 revenue/EPS goes from QR2.6bn/QR14.37 to QR2.3bn/QR12.07. The aforementioned changes in tariffs/offtakes came as a surprise and we have adjusted our model accordingly.

- **Our forward revenue/EPS estimates decrease by an average of 12%/16%.** Our forward EBITDA estimates have also come down by 15%. Moving beyond the 13% decline, 16% fall and 23% decline in revenue, net income and EBITDA, respectively, in 2019, our model shows a CAGR (2019-2023) of 1.6% in revenue, 3.7% in earnings and 1.5% in EBITDA as we grow the business by inflation-related increases. We also note RAF B1's current contracts ends in August 2022 and we have modeled in another decline in tariff rates for that project. Our JV income estimates also factor in Umm Al Houl's increase in water capacity by 45% from 136.5 MIGD to 198 MIGD in 2021; this project is expected to cost \$400mn and QEWS retains a 60% stake in this plant.
- **We have also kept our DPS flat at QR7.75 over our forecast period vs. our previous estimate of modest growth from 2021 onward.**

QNB FS Current Estimates Vs. Previous Estimates

Income Statement (QR mn) Particulars	Current				Previous											
	2018	2019e	2019e	Δ	2020e	2020e	2020e	Δ	2021e	2021e	2021e	Δ	2022e	2022e	2022e	Δ
Revenue	2,601.491	2,256.810	2,559.270	-11.8%	2,299.429	2,609.130	-11.9%		2,344.236	2,661.687	-11.9%		2,377.028	2,716.857	-12.5%	
Cost of Sales (Excluding Depreciation)	(1,120.129)	(1,071.985)	(1,190.061)	-9.9%	(1,092.229)	(1,226.291)	-10.9%		(1,113.512)	(1,250.993)	-11.0%		(1,129.088)	(1,276.923)	-11.6%	
Gross Profit	1,481.362	1,184.825	1,369.209	-13.5%	1,207.200	1,382.839	-12.7%		1,230.724	1,410.694	-12.8%		1,247.940	1,439.934	-13.3%	
General & Administrative Expenses	(176.408)	(178.172)	(178.172)	0.0%	(182.626)	(182.626)	0.0%		(187.192)	(187.192)	0.0%		(191.872)	(191.872)	0.0%	
EBITDA	1,304.954	1,006.653	1,191.037	-15.5%	1,024.574	1,200.212	-14.6%		1,043.532	1,223.502	-14.7%		1,056.068	1,248.062	-15.4%	
Depreciation	(279.525)	(288.333)	(265.333)	8.7%	(292.333)	(269.333)	8.5%		(296.333)	(273.333)	8.4%		(300.333)	(277.333)	8.3%	
Amortization	(7.949)	(7.949)	(7.949)	0.0%	(7.949)	(7.949)	0.0%		(7.949)	(7.949)	0.0%		(7.949)	(7.949)	0.0%	
EBIT	1,017.480	710.371	917.755	-22.6%	724.292	922.930	-21.5%		739.250	942.220	-21.5%		747.786	962.780	-22.3%	
Finance Costs	(226.835)	(232.754)	(243.931)	-4.6%	(209.115)	(234.039)	-10.6%		(199.250)	(224.067)	-11.1%		(188.826)	(213.528)	-11.6%	
Interest Income & Share of Interest Income from JVs	112.386	118.005	123.625	-4.5%	123.906	135.987	-8.9%		130.101	149.586	-13.0%		136.606	164.544	-17.0%	
Finance Costs - Net	(114.449)	(114.749)	(120.307)	-4.6%	(85.209)	(98.052)	-13.1%		(69.149)	(74.482)	-7.2%		(52.220)	(48.984)	6.6%	
Dividend Income and Gain on Sale of AFS	38.049	60.000	80.000	-25.0%	61.815	84.000	-26.4%		64.905	88.200	-26.4%		68.151	92.610	-26.4%	
Other & Misc. Income / Expense	81.914	60.000	81.914	-26.8%	60.000	81.914	-26.8%		60.000	81.914	-26.8%		60.000	81.914	-26.8%	
Share of profits of JV Companies	542.190	603.882	603.882	0.0%	596.750	618.978	-3.6%		639.472	634.453	0.8%		655.458	650.314	0.8%	
Profit before Tax	1,565.184	1,319.504	1,563.244	-15.6%	1,357.646	1,609.770	-15.7%		1,434.477	1,672.305	-14.2%		1,479.174	1,738.634	-14.9%	
Tax																
Profit after Tax	1,565.184	1,319.504	1,563.244	-15.6%	1,357.646	1,609.770	-15.7%		1,434.477	1,672.305	-14.2%		1,479.174	1,738.634	-14.9%	
Minority Interest	(28.597)	(29.108)	(28.562)	1.9%	(29.950)	(29.412)	1.8%		(31.645)	(30.554)	3.6%		(32.631)	(31.766)	2.7%	
Profit for Equity Holders	1,536.587	1,290.395	1,534.682	-15.9%	1,327.697	1,580.359	-16.0%		1,402.833	1,641.751	-14.6%		1,446.544	1,706.868	-15.3%	
Net Profit Margin	59.1%	57.2%	60.0%		57.7%	60.6%			59.8%	61.7%			60.9%	62.8%		
Shares O/S (mn)	110	110	110		110	110			110	110			110	110		
Basic and Diluted EPS	13.97	11.73	13.95	-15.9%	12.07	14.37	-16.0%		12.75	14.93	-14.6%		13.15	15.52	-15.3%	
DPS	7.75	7.75	7.75	0.0%	7.75	7.75	0.0%		7.75	8.00	-3.1%		7.75	8.25	-6.1%	
Dividend Payout Ratio	55.5%	66.1%	55.5%		64.2%	53.9%			60.8%	53.6%			58.9%	53.2%		
Margins/Ratios	2018	2019e	2019e		2020e	2020e			2021e	2021e			2022e	2022e		
Cost of Sales	43.1%	47.5%	46.5%		47.5%	47.0%			47.5%	47.0%			47.5%	47.0%		
Gross Margin	56.9%	52.5%	53.5%		52.5%	53.0%			52.5%	53.0%			52.5%	53.0%		
General & Administrative Expenses (% of Sales)	6.8%	7.9%	7.0%		7.9%	7.0%			8.0%	7.0%			8.1%	7.1%		
EBITDA Margin	50.2%	44.6%	46.5%		44.6%	46.0%			44.5%	46.0%			44.4%	45.9%		
EBIT Margin	39.1%	31.5%	35.9%		31.5%	35.4%			31.5%	35.4%			31.5%	35.4%		

Source: QNB FS estimates

Valuation and Key Ratios

Valuation Metrics

Particulars	2014	2015	2016	2017	2018	2019e	2020e	2021e	2022e	2023e
Valuation										
EV/EBITDA - Consolidated	13.9	13.1	12.5	12.7	14.6	19.0	18.2	17.4	16.7	16.1
EV/EBIT	19.9	18.4	16.8	18.0	18.8	27.0	25.8	24.6	23.6	22.7
P/E	11.6	11.8	12.0	11.0	11.5	13.7	13.3	12.6	12.2	11.9
P/CF	8.0	9.6	8.6	10.6	8.5	11.8	11.3	11.5	11.3	11.1
P/BV	2.6	2.4	2.1	2.0	1.7	1.7	1.6	1.5	1.5	1.4
Dividend Yield	4.7%	4.7%	4.7%	4.8%	4.8%	4.8%	4.8%	4.8%	4.8%	4.8%
FCF Yield	(2.7%)	4.6%	6.9%	9.1%	5.9%	6.7%	7.9%	7.7%	7.8%	8.0%

Source: Bloomberg, QNB FS estimates

Peer Comparison

Company	Mcap	P/E		EV/EBITDA		P/CF		ROE		EBITDA Margin		Dividend Yield	
	\$ mn	2019e	2020e	2019e	2020e	2019e	2020e	2019e	2020e	2019e	2020e	2019e	2020e
SAUDI ELECTRICITY CO	17,754	59.2	40.5	9.6	9.2	-5.98	-7.58	2.3%	3.0%	35.1%	35.4%	4.38	4.38
TAQA MOROCCO	2,111	18.6	18.6	8.4	8.2	9.6	8.3	19.8%	19.7%	41.8%	41.4%	4.84	4.83
ABU DHABI NATIONAL ENERGY CO	1,404	7.1	7.1	7.7	7.5	1.3	1.3	11.2%	14.3%	51.0%	50.0%	n.a	n.a
TABREED	1,139	9.4	9.4	10.1	9.8	7.7	7.6	9.8%	9.8%	46.0%	45.6%	6.30	6.49
MONTAUK ENERGY HOLDINGS LTD	391	9.4	14.9	8.6	7.3	n.a.	n.a.	29.8%	26.6%	48.7%	42.0%	2.61	3.53
SEMBCORP SALALAH POWER & WA	273	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a	n.a
KENYA ELECTRICITY GENERATING	395	2.8	2.8	7.1	6.0	-6.7	21.2	3.9%	7.0%	63.7%	64.7%	7.92	11.14
LYONNAISE DES EAUX DE CASABL	389	22.1	22.1	4.6	4.2	8.3	7.3	8.2%	8.7%	14.5%	15.8%	5.39	5.60
SEVERN TRENT PLC	5,760	16.7	14.5	11.6	11.3	51.6	29.1	26.3%	21.8%	51.5%	50.9%	4.86	5.18
UNITED UTILITIES GROUP PLC	6,592	17.2	13.5	11.8	11.3	15.4	11.8	12.2%	9.3%	59.1%	59.7%	5.37	5.54
TATA POWER CO LTD	2,491	9.2	10.5	10.0	9.3	3.9	4.7	9.3%	9.6%	20.6%	21.1%	2.02	2.45
CESC LTD	1,374	7.3	7.9	6.9	6.6	5.1	6.0	11.6%	11.7%	26.4%	27.1%	2.41	2.35
NTPC LTD	18,346	9.8	9.8	9.5	8.2	-11.4	-46.3	10.3%	11.4%	27.5%	28.6%	3.34	3.71
EDP - ENERGIAS DO BRASIL SA	2,872	11.7	11.7	6.9	6.3	-29.7	46.8	11.3%	11.2%	19.5%	20.4%	4.00	4.68
Peer Group Average		15.4	14.1	8.7	8.1	4.1	7.5	12.8%	12.6%	38.9%	38.7%	4.5%	5.0%
Peer Group Normalized Av.		12.6	12.7	8.7	8.2	2.7	9.0	12.2%	12.2%	38.8%	38.4%	4.4%	4.6%
Peer Group Normalized Av.2		12.2	12.3	8.6	8.0	2.9	8.5	11.5%	11.7%	38.7%	38.0%	4.3%	4.7%

QATAR ELECTRICITY & WATER CO	4,863	13.7	13.3	19.0	18.2	11.8	11.3	12.3%	12.1%	44.6%	44.6%	4.81	4.81
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Source: Bloomberg, QNB FS estimates

Key Growth Rates/CAGRs/Ratios

Particulars	2014	2015	2016	2017	2018	2019e	2020e	2021e	2022e	2023e	CAGR ('19-'23)
Growth Rates											
Revenue	(0.2%)	2.9%	4.0%	(1.0%)	(15.3%)	(13.2%)	1.9%	1.9%	1.4%	1.2%	1.6%
Gross Profit	(1.8%)	1.9%	3.6%	(3.3%)	(15.8%)	(20.0%)	1.9%	1.9%	1.4%	1.2%	1.6%
EBITDA - Consolidated	(2.5%)	5.4%	2.8%	(4.9%)	(15.8%)	(22.9%)	1.8%	1.9%	1.2%	1.0%	1.5%
EBIT	(3.5%)	7.3%	7.2%	(9.3%)	(7.2%)	(30.2%)	2.0%	2.1%	1.2%	0.9%	1.5%
JV Income	3.6%	4.1%	(25.1%)	85.4%	(4.4%)	11.4%	(1.2%)	7.2%	2.5%	2.5%	2.7%
PBT	11.0%	(2.0%)	(1.9%)	8.8%	(4.5%)	(15.7%)	2.9%	5.7%	3.1%	3.0%	3.7%
PAT/EPS	10.5%	(1.9%)	(1.7%)	9.5%	(4.9%)	(16.0%)	2.9%	5.7%	3.1%	3.0%	3.7%
DPS	10.0%	0.0%	0.0%	3.3%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
CFPS	30.7%	(16.6%)	11.7%	(19.1%)	24.2%	(27.4%)	4.6%	(2.2%)	2.0%	2.0%	1.6%
FCFPS	NM	NM	50.5%	30.9%	(35.1%)	13.0%	18.3%	(2.5%)	2.3%	2.3%	4.8%
Operating Ratios											
Gross Margin	59.5%	58.9%	58.7%	57.3%	56.9%	52.5%	52.5%	52.5%	52.5%	52.5%	
EBITDA Margin - Consolidated	51.8%	53.1%	52.5%	50.4%	50.2%	44.6%	44.6%	44.5%	44.4%	44.3%	
EBIT Margin	36.3%	37.8%	38.9%	35.7%	39.1%	31.5%	31.5%	31.5%	31.5%	31.4%	
Net Margin	52.8%	50.3%	47.5%	52.6%	59.1%	57.2%	57.7%	59.8%	60.9%	61.9%	
Finance Ratios											
Debt-Equity Ratio	0.8	0.7	0.7	0.7	0.7	0.6	0.5	0.5	0.4	0.4	
Net Debt-Equity Ratio	0.5	0.4	0.4	0.3	0.3	0.3	0.2	0.1	0.1	0.1	
Interest Coverage	9.7	9.4	8.1	6.1	4.5	3.1	3.5	3.7	4.0	4.2	
Return Ratios											
ROIC	8.8%	9.2%	8.5%	7.4%	5.9%	4.4%	4.4%	4.4%	4.4%	4.3%	
ROE	22.6%	20.4%	17.8%	18.0%	14.7%	12.3%	12.1%	12.1%	11.9%	11.7%	
ROA	11.8%	11.2%	9.7%	10.2%	8.5%	7.5%	7.6%	7.9%	8.0%	8.1%	
FCF Yield	-2.7%	4.6%	6.9%	9.1%	5.9%	6.7%	7.9%	7.7%	7.8%	8.0%	
Liquidity Ratios											
Current Ratio	1.2	1.5	2.1	2.3	1.6	1.3	1.4	1.6	1.8	2.0	
Quick Ratio	1.1	1.4	1.9	2.2	1.6	1.3	1.4	1.5	1.7	1.9	

Source: Bloomberg, QNB FS estimates

Detailed Financial Statements

Income Statement (In QR mn)	FY2018	FY2019e	FY2020e	FY2021e
Revenue	2,601	2,257	2,299	2,344
Cost of Sales, Excluding Depreciation	(1,120)	(1,072)	(1,092)	(1,114)
Gross Profit	1,481	1,185	1,207	1,231
General & Administrative Expenses	(176)	(178)	(183)	(187)
EBITDA	1,305	1,007	1,025	1,044
Deferred Income	0	0	0	0
Depreciation & Amortization	(287)	(296)	(300)	(304)
EBIT	1,017	710	724	739
Finance Costs, Net	(189)	(173)	(147)	(134)
Dividend Income & Gain on Sale of AFS	112	118	124	130
Other & Miscellaneous Income/Expense & Share of Profits from JVs	624	664	657	699
Share of Associates	0	0	0	0
Profit Before Tax	1,565	1,320	1,358	1,434
Income Tax Expense	0	0	0	0
Profit After Tax (Continuing Operations)	1,565	1,320	1,358	1,434
Discontinued Operations				
Minority Interest	(29)	(29)	(30)	(32)
Profit for Shareholders	1,537	1,290	1,328	1,403
EPS (QR)	13.97	11.73	12.07	12.75

Source: Company data, QNB FS estimates

Balance Sheet (In QR mn)	FY2018	FY2019e	FY2020e	FY2021e
Non-Current Assets				
Property, Plant & Equipment	5,750	5,562	5,370	5,173
Available-for-Sale Investments	1,559	1,529	1,529	1,529
Finance Lease Receivables	1,118	1,000	895	801
JV Loans and Investments in JVs	4,718	5,209	5,551	5,912
Other Non-Current assets	150	127	119	111
Total Non-Current Assets	13,294	13,427	13,463	13,526
Current Assets				
Finance Lease Receivables & Others	139	143	143	143
Inventories	142	132	135	137
Accounts Receivables & Prepayments	444	402	409	417
Cash and Short-Term Deposits	4,118	3,060	3,319	3,528
Total Current Assets	4,844	3,737	4,006	4,225
Total Assets	18,137	17,164	17,469	17,751
Equity				
Equity to the Parent	10,456	10,522	10,997	11,548
Minority Interest	258	265	273	281
Total Equity	10,713	10,787	11,270	11,829
Non-Current Liabilities				
Loans and Borrowings	4,366	3,474	3,318	3,154
Employees' End of Service Benefits	69	71	73	75
Other Payables		22	22	22
Derivatives	16	16	16	16
Total Non-Current Liabilities	4,451	3,583	3,429	3,266
Current Liabilities				
Accounts Payables & Others	525	473	554	549
Loans and Borrowings	2,444	2,316	2,212	2,102
Derivatives	5	5	5	5
Total Current Liabilities	2,973	2,793	2,770	2,656
Equity and Liabilities	18,137	17,164	17,469	17,751

Source: Company data, QNB FS 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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