QEWS Alert – 3Q2020 Net Income Beats Forecast on JV Income Growth; Accumulate

- **QEWS reports 3Q2020 earnings that exceeds our modeled estimate –** QEWS' net profit rose 13.0% YoY and 9.8% QoQ in 3Q2020 to QR373.7mn, ahead of our estimate of QR346.1mn (variation of 8.0%). Overall top-line and costs performance remained generally consistent with our modeled estimates with majority of the outperformance due to better-than-expected JV income. We believe seasonality drove this growth in JV income on a sequential basis.
- **Total 3Q2020 revenue (power+water+lease interest) of QR696.0mn (8.4% YoY, 6.2% QoQ) was in-line with our forecast of QR669.5mn (divergence of 4.0%).** As has been our view throughout 2020 and highlighted in our preview, 3Q2020 marked the fourth consecutive quarter of YoY revenue increases, with QEWS' top-line registering gains of 3.0%, 11.1% and 8.5% in 4Q2019, 1Q2020 and 2Q2020, respectively, after posting yearly declines through 1Q2019-3Q2019. .
- **Growth in JV income, along with lower finance charges, helped boost profitability.** Gross margin came in at 43.6% in 3Q2020, which was modestly lower than 45.6% in 3Q2019 and below the 48.1% metric posted in 2Q2020. EBITDA margin at 38.5%, while modestly below last year's 39.0%, was also below the 42.5% recorded in 2Q2020; EBITDA margin was aided by lower G&A expenses on a YoY/QoQ basis and sequentially lower D&A expenses but were hurt by lower gross margins vs. 3Q2019 and 2Q2020. Operating margin improved modestly YoY, increasing from 27.9% in 3Q2019 to 28.2% in 3Q2020; operating margin declined QoQ vs. 31.2% in 2Q2020.
- **Earnings continue to enjoy better YoY comparisons as we progress through 2020.** As we have noted previously, RAF B, which already witnessed lowered tariffs under a 12-year contract extension from July 2018, also faces lower offtake in 2019/2020 given Umm Al Houl's ramp up. Moreover, RAF B1/B2 are going through a contractually agreed dip in tariff rates. Costs have also increased beyond modeled expectations given higher-than-expected gas costs for RAF B's renewal. *However, with these items already affecting 2019 performance, YoY comparisons continue to look better in 2020. This was evident in 1H2020 earnings performance in our view and the trend continued in 3Q2020 as well.*
- **We remain Accumulate on QEWS with a price target of QR17.00.** We continue to like the company as a long-term play with a relatively defensive business model, especially in light of current market conditions. The near-term impact of the COVID-19 pandemic could remain muted on QEWS' business model as the company is paid based on power and water availability and is not affected by the vagaries of end demand. QEWS still enjoys decent EBITDA margins and dividend/FCF yields. LT catalysts (which are not in our model) abound, including additional domestic expansions (like Facility E in 2022-2023; Siraj solar project in 2021-2022, etc.). Nebras remains on the hunt for growth with a goal of increasing its net capacity to 6 GW by 2023 from 1.7 GW in September 2019. However, beyond Paiton (Indonesia), we do not have color on other major Nebras projects, which could lead to growth relative to our model.

QNB FINANCIAL SERVICES

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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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