

QGTGS Alert – 2Q2022 Operationally In-Line/Better But Modest Earnings Miss On Finance Charges

- **Nakilat reports a modest miss in 2Q2022 bottom-line but operationally delivers another impressive quarter.** QGTGS' 2Q2022 net income of QR347.8mn increased 10.4% YoY but declined 8.9% QoQ, coming in 5.4% lower than our estimate of QR367.8mn. **(1) Revenue from wholly-owned ships** of QR887.3mn (0.3% YoY, 1.5% QoQ) was in-line with our estimate of QR879.2mn (variation of 0.9%). The sequential increase in wholly-owned ship revenue is likely driven by higher operating days in 2Q2022 vs. 1Q2022. **(2) Adjusted revenue** (wholly-owned ships + marine & agency services + JV income) of QR1.07bn (7.1% YoY, 2.1% QoQ) was also in-line with our estimate of QR1.03bn (divergence of 3.2%) and was driven by the strength in JV income. **(3) EBITDA** of QR698.9mn (1.0% YoY, 2.8% QoQ) was 2.4% ahead of our forecast of QR682.5mn given improvement in cash gross margins (79.8% vs. our model of 78.8%); EBITDA performance was aided by lower-than-expected direct operating costs of the wholly-owned fleet and an upside in marine & agency services. While **G&A** expenses of QR23.7mn (4.5% YoY, 15.4% QoQ) was 12.5% above our estimate of QR21.0mn, G&A expenses for 1H2022 of QR44.2mn was moderately lower than 1H2021's QR44.6mn due to continued improvements (along with some timing-related variation). **(4) Adjusted EBITDA** of QR862.9mn (9.5% YoY, 2.9% QoQ) was 4.6% above our estimate of QR825.2mn. **(5) JV income** of QR164.0mn (70.5% YoY, 3.2% QoQ) was 14.9% above our estimate of QR142.7mn. Improving shipyard performance (which posted net losses of QR36.2mn and QR25.5mn in 2021 and 2020, respectively), along with addition of the 3rd/4th LNG vessels in QGTGS's Global Shipping JV in Oct. 2021/Jan. 2022, led to this increase. **(6) Finally finance costs** came in at QR306.0mn (15.5% YoY, 17.7% QoQ), and was 18.9% ahead of our estimate of QR257.4mn. Management attributed this increase to one-off write-off of legacy financing costs due to refinancing and an increase in LIBOR rates on the unhedged portion of QGTGS' debt, offset by scheduled repayment of loans.
- **2022 could be a watershed year for Nakilat if it is selected as one of the ship owners involved in Qatar's massive LNG expansion program.** We remind investors that QatarEnergy is expanding Qatar's LNG capacity from 77 MTPA to 110 MTPA (first production: 4Q2025) and further to 126 MTPA a couple of years later. To cater to this expansion, back in April/June 2020, QatarEnergy signed major LNG shipbuilding capacity agreements with Chinese and South Korean companies to build 100+ LNG vessels worth +QR70bn. Furthermore, in 1Q2021, QatarEnergy issued an invitation to tender package to ship owners for the chartering of LNG carriers in relation to this project; QatarEnergy intends to assign selected ship owners from this tender to the shipyards' construction slots reserved in China and South Korea. In October and November of 2021, QatarEnergy moved ahead with the construction of ten LNG ships (four in China/six in South Korea). We do note that already on April 12, 2022, QatarEnergy announced that it awarded its first batch of time-charter parties (TCPs) with a subsidiary of Mitsui O.S.K Lines (MOL) for the long-term charter and operation of four LNG ships. In a statement, HE the Minister of State for Energy Affairs, Saad Sherida al-Kaabi, also the President and CEO of QatarEnergy, stated that he expected to announce similar contracts in the near future. In early June 2022, South Korean Shipbuilders announced some details of construction orders involving six ships (174k cm each) at a cost of ~\$215mn/ship. *Considering Nakilat's strategic importance and impressive track record in Qatar's existing LNG shipping value chain, we expect QGTGS to be a major beneficiary and secure a meaningful share of new contracts. We also estimate that every incremental vessel (@100%) adds ~1% to QGTGS' target price (for details, please see our [report](#)) and an award of 20-30 ships could significantly increase our price target and estimates. Given typical lead-times for LNG ship construction, we should expect to hear about final ship owner selections later in 2022/early 2023.*
- **We remain bullish on Nakilat and consider it as the best avenue for equity investors to participate in the LT growth expected in Qatar's LNG sector.** Irrespective of the volatility of the LNG shipping market, Nakilat's business should remain relatively unaffected given the LT nature of its charters. QGTGS' fleet continues to provide Nakilat with stable, contractually sustainable cash flow that allow for a healthy residual income stream for equity investors after providing for debt service. Moreover, the 40-year life of QGTGS' vessels vs. maximum debt life of 25 years (last debt maturing 2033), could allow for value-enhancement. Near-term, addition of 4 LNG vessels (final vessel added in Jan. 2022) via Global Shipping, should help 2022 earnings growth. *We remain Accumulate on QGTGS with a price target of QR4.100 and will likely revise our price target when we update our numbers in the near future.*

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Income Statement							
In QR mn Except Otherwise Noted	2Q2021	1Q2022	2Q2022	2Q2022e	A Vs. E	YoY	QoQ
Revenue from Wholly-Owned Vessels	884.550	873.928	887.345	879.220	0.9%	0.3%	1.5%
Operating Costs	(184.391)	(184.165)	(179.265)	(186.395)	-3.8%	-2.8%	-2.7%
Gross Profit	700.159	689.763	708.080	692.825	2.2%	1.1%	2.7%
<i>Gross Margin</i>	79.2%	78.9%	79.8%	78.8%			
Income from Marine and Agency Services	14.513	10.785	14.504	10.731	35.2%	-0.1%	34.5%
General and Administrative Expenses	(22.664)	(20.535)	(23.689)	(21.048)	12.5%	4.5%	15.4%
EBITDA	692.008	680.013	698.895	682.508	2.4%	1.0%	2.8%
Depreciation & Amortization	(220.850)	(217.404)	(222.006)	(220.665)	0.6%	0.5%	2.1%
EBIT	471.158	462.609	476.889	461.843	3.3%	1.2%	3.1%
<i>EBIT Margin</i>	53.3%	52.9%	53.7%	52.5%			
Share of Operating Profits from Joint Ventures	96.205	158.949	163.991	142.736	14.9%	70.5%	3.2%
Finance Costs	(265.029)	(259.967)	(306.002)	(257.367)	18.9%	15.5%	17.7%
Interest, Dividend income & Profit from Islamic Banks	13.108	20.373	13.260	20.679	-35.9%	1.2%	-34.9%
Vessel Sub-Chartering & Other Income	-						
Profit Before Tax	315.442	381.964	348.138	367.891	-5.4%	10.4%	-8.9%
Profit After Tax	315.442	381.964	348.138	367.891	-5.4%	10.4%	-8.9%
Minority Interest	(0.361)	(0.129)	(0.332)	(0.124)	167.2%	-8.0%	157.4%
Net Income to Equity	315.081	381.835	347.806	367.766	-5.4%	10.4%	-8.9%
<i>Net Profit Margin</i>	35.6%	43.7%	39.2%	41.8%			
EPS (QR)	0.06	0.07	0.06	0.07	-5.4%	10.4%	-8.9%
Adjusted EBITDA	788.213	838.962	862.886	825.244	4.6%	9.5%	2.9%
Adjusted Revenue	995.268	1,043.662	1,065.840	1,032.687	3.2%	7.1%	2.1%

Particulars	2Q2021	1Q2022	2Q2022	2Q2022e
Adj. EBITDA Margin	79.2%	80.4%	81.0%	79.9%
Gross Margin	79.2%	78.9%	79.8%	78.8%
EBIT Margin	53.3%	52.9%	53.7%	52.5%
G & A % of Sales	2.6%	2.3%	2.7%	2.4%
Depreciation & Amortization % of Sales	25.0%	24.9%	25.0%	25.1%

Recommendations	
<i>Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price</i>	
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	
<i>Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals</i>	
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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