



CURRENT PRICE	QAR 25.30
FAIR VALUE	QAR 44.35
RECOMMENDATION	BUY

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EMPIRE UNDER CONSTRUCTION

THE COUNTRY OF GAS

Possessing 13.8% of the earth's proven natural gas (NG) reserves, Qatar is the biggest NG exporter in the world. Currently, Qatar does not use underground pipelines to transport NG. It uses floating pipelines: vessels, mainly those of Nakilat.

LARGEST LNG TRANSPORTATION COMPANY

With an expected 2010 Liquefied Natural Gas (LNG) fleet of 54 vessels, Qatar Gas Transport Company, commonly known as Nakilat, will be the largest LNG transportation company in the world, with a market share of more than 17%.

TRANSPORTING HALF OF THE QATARI LPG

In addition to its LNG fleet, Nakilat has four Liquefied Petroleum Gas (LPG) vessels and aims to quadruple its fleet in order to be able to transport half of the Qatari LPG production, expected to be 12 million tons in 2014.

STABLE CASH FLOW

All the LNG vessels are long-term chartered, and so they generate stable revenues. In addition, Nakilat entered into derivatives contracts to fix the interest expenses on its QAR 23 billion debt, resulting in lower risk.

REVENUES STARTING TO BE RECORDED

As Nakilat starts to receive its vessels, operating revenues will be recognized as we go forward. Vessels are still partly operated, and so they contributed only a small portion of the company's revenues in the past quarters. However, quarterly revenues are expected to increase gradually till 2010, when the company's fleet will be fully operated.

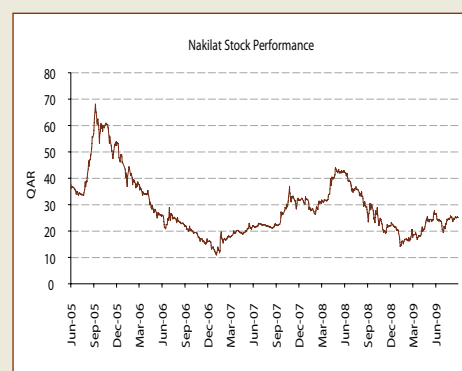
UNDERVALUED STOCK

Nakilat is currently traded at a trailing PE of 51.45. However, we expect a PE 09 of 24.61 and PE 10 of 10.08.

Based on our valuation, we estimate a fair value of QAR 44.35, indicating an upside potential of 75%.

STOCK DATA

Market Cap (QAR million)	13,952
Market Cap (USD million)	3,767
Shares Outstanding (million)	553.67
Free Float	50%
Av. Monthly Liquidity (QAR million)	915
52-week High (QAR)	28.90
52-week Low (QAR)	14.20
Trailing PE	51.45
PB	2.28



Year	2008	2009 E	2010 E	2011 E
Revenues (QAR million)	287	1,989	3,612	3,664
Net Income (QAR million)	214	571	1,395	1,428
EPS (QAR)	0.23	1.03	2.51	2.57
ROE	2%	9%	27%	20%

SECTOR COVERAGE

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EXECUTIVE SUMMARY

Qatar Gas Transport Company was established in 2004 with the aim of becoming an integral link of the LNG supply chain for Qatar.

With about 13.8% of the earth's proven natural gas reserves, Qatar is the biggest NG exporter in the world. In 2008, Qatar produced 76.6 billion cubic meters of NG, and it is expected to produce about 106 billion cubic meters by 2010.

Currently, Qatar does not use underground pipelines to transport NG. It uses floating pipelines: vessels, mainly those of Nakilat.

Nakilat is expanding its fleet. By 2010, it will have 54 LNG vessels, the largest fleet in the world. The company will fully own 25 ships and will have a 43% ownership, on average, in the remaining ones.

The company plans to more than quadruple its LPG fleet currently consisting of four vessels. Besides, it will expand further in the bulk sector, by acquiring four cargo ships.

Nakilat does not have vessels, it has contracted vessels. The company's LNG fleet is chartered on a long-term basis (up to 25 years). Thus, Nakilat's utilization rate and revenue stream are expected to be little affected by the daily market changes.

After completing its expansion, Nakilat will have the newest fleet in the world. This will be positively reflected in the charter rates. In addition, it has entered into a strategic alliance with Shell International in order to operate the vessels.

The company has launched a ship yard project to construct and maintain ships and offshore structures. Construction of the first marine vessel is expected to start in mid-2010.

Qatar Gas Transport has entered into an interest rate Swap allowing it to transfer a part of its variable rate loans into fixed rate. By doing this, the company is trying to match its revenues with its costs, and thereby decreasing its risk.

On the other hand, some minor risks still exist, namely lack of financial transparency, financing risk from changes in interest rate on loans, and market risk related to the valuation of its Available for Sale portfolio.

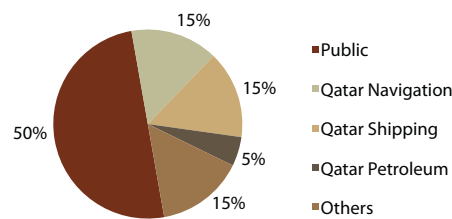
COMPANY OVERVIEW

With no established underground pipeline chain, Qatar needs vessels to export its natural gas

In 2003, Qatar started expanding its natural gas production with the aim of increasing the volume exported. Yet, because of its geographical location, Qatar needs time to construct an underground pipeline chain to export the gas. In addition, pipelines could not reach all markets, especially the United States and the United Kingdom, the biggest importers. Thus, Qatar needs floating pipelines in the form of vessels. However, existing national shipping companies, including Qatar Navigation and Qatar Shipping, did not have the required capacity to ship the LNG outside the country. Therefore, the establishment of a company that specialized in exporting Qatar's main natural resource was a must.

In 2004, Qatar Gas Transport was founded with the aim of becoming an integral link of the LNG supply chain for Qatar. Qatar Gas Transport, commonly known as Nakilat, is a joint stock company owned 50% by its founding shareholders and 50% by the public as a result of an IPO in 2005.

Chart 1: Nakilat Ownership



Source: Nakilat website

Nakilat will be the largest LNG company in the world, by 2010

Nakilat is building a huge LNG fleet which is expected to reach 54 vessels by 2010. Of these, the company will fully own 25 ships; it will partially own the remaining ones, with an average ownership stake of 43%. These vessels are expected to be fully operational by 2010. Moreover, Nakilat has the option to purchase additional two new wholly-owned carriers.

Expanding in complementary industries

In March 2008, the company entered into a joint venture agreement with Qatar Shipping and formed the Gulf LPG Transport Company. This equally owned company took delivery of four vessels responsible to transport LPG. Recently, Qatar Gas Transport managing director, Mohammad Ghannam, said that Nakilat may add up to 17 LPG vessels in order to meet the increase in Qatar's LPG output.

Furthermore, Qatar Gas Transport is trying to diversify its business lines by establishing a facility for the construction and maintenance of marine and offshore structures, in close collaboration with Qatar Petroleum. This new facility, which is located in Ras Laffan, is divided into five phases, and the first two phases of construction are scheduled to be completed in late 2009.

In addition, Nakilat has a number of joint ventures that offer different marine services. They include Nakilat-Keppel Offshore & Marine, which is responsible for developing and managing a world-class shipyard facility in the Port of Ras Laffan; Nakilat Agency Company Limited, which acts as the exclusive agent for all ships calling at the Port of Ras Laffan; and Nakilat Svitserwijmuller W.L.L., which owns and operates tug boats, pilot boats and other harbor craft at Ras Laffan Port.



INDUSTRY OVERVIEW

QATAR AND LNG

Qatar, the State

Comprising an area of 11,586 km², the State of Qatar consists of a peninsula projecting northward into the Persian Gulf, extending 187 km from the north to the south, and 90 km from the east to the west.

Table 1: Population Statistics, as of 2008

Population	1,448,449
Annual Growth	0.86%
Labor Force	1,120,000
Unemployment	0.6%

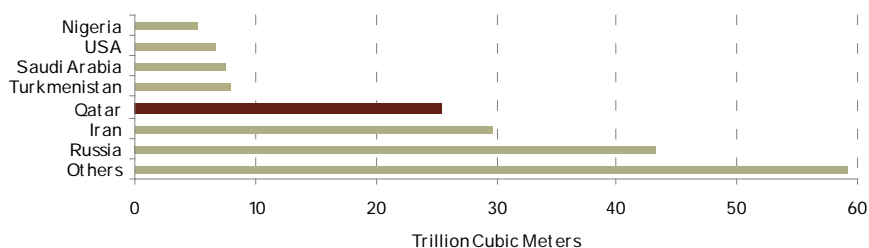
Source: Qatar Statistics Authority (QSA)

Qatar has the third largest NG proven reserves in the globe

Oil and Gas Reserves

Theoretically, Qatar could be divided horizontally into two parts, the north and the south. The raw material wealth of Qatar is highly concentrated in the upper side, namely the North Field, which covers an area of over than 6,000 km². Qatar has proven reserves of 27.3 billion barrels of oil, representing 2.2% of global proven reserves. In addition, it has 25.46 trillion cubic meters of natural gas reserves, representing 13.8% of the earth's proven natural gas reserves. The majority of these reserves are located in the North Field which is the largest non-associated natural gas field in the world.

Chart 2: Global Natural Gas Proved Reserves



Source: BP Statistical Review, June 2009



Gas is becoming the largest contributor to Qatar's GDP

The Economy

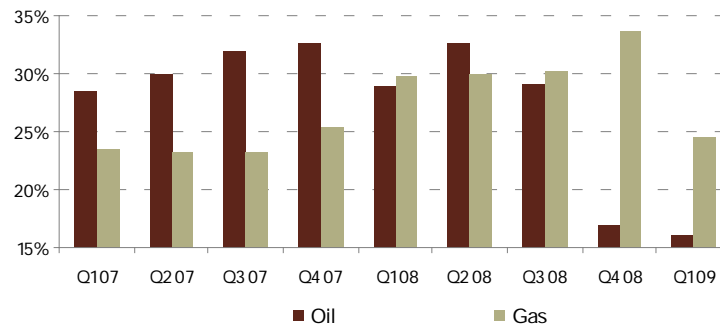
For a long time, oil was the main source of income for Qatar. It used to be the first contributor to the state's GDP with a stake of about 30%. However, starting Q3 08, natural gas revenues have exceeded those from oil for the first time, mainly due to the huge increase in the natural gas volume exported.

Table 2: 2008 Economic Statistics

Currency	Qatari Riyal (QAR)
Exchange Rate QAR/USD	3.64
GDP billion QAR	365.5
Oil Production	27%
Gas Production	31%
Real GDP Growth	16%
GDP per Capita QAR	253,819

Source: Qatar Statistics Authority (QSA)

Chart 3: Oil and Gas Contribution to Qatar GDP



Source: QSA

Gas Projects

Investing in natural gas started decades ago. Since 1980, the government has increased its emphasis on the natural gas sector in order to complement, or even at a later stage replace, oil as the main source of income. From that time, plans were put into action and projects were started to explore Qatar's new export commodity. In 1984, Qatargas was established in order to operate three Liquefied Natural Gas (LNG) trains with a design capacity of 2 million tons (equivalent to 2.76 billion cubic meters of natural gas) per year each (Qatargas 1). In 1996, Qatargas 1 started production and the first LNG cargo was delivered to Japan. That was a turning point in the history of Qatar. Currently, two companies are responsible for gas exploration, Qatargas and Rasgas.

The first LNG production facility in Qatar was established in 1984



Table 3: Qatar Expected LNG Production by Trains

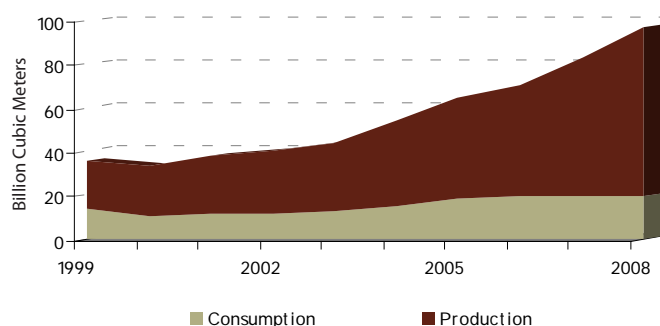
Project	Train - Production Line	LNG Consolidated Capacity million tons per year	Equivalent Natural Gas Capacity billion cubic meters per year	Import Markets
Qatargas 1	1,2&3	10	13.8	Japan & Spain
Qatargas 2	4&5	15.6	21.5	UK
Qatargas 3	6	7.8	10.8	US
Qatargas 4	7	7.8	10.8	US & Europe
Rasgas 1	1&2	6.6	9.1	Korea
Rasgas 2	3,4&5	14.1	19.5	Europe & Asia
Rasgas 3	6&7	15.6	21.5	US & Asia

Sources: Qatargas, Rasgas and Audi Capital - KSA

Production and Consumption

In 2008, Qatar produced 76.6 billion cubic meters of natural gas (equivalent to 56 million tons of LNG), according to the BP Statistical Review of World Energy. In 2009, new capacity is being added, mainly by Qatargas trains 5. At the same time, one of the biggest production lines, Qatargas train 4, will be closed for a few weeks in Q4 09 for maintenance. By end-2010, Qatar aims to produce 106 billion cubic meters of natural gas (or 77 million tons of LNG), about 82% of which are expected to be exported to outside markets.

Chart 4: Qatar Natural Gas Production and Consumption



Source: BP

LNG Exports

2006 was a very important year for Qatar. In that year, the small state exported 22.5 million tons of LNG and overtook Indonesia, which had dominated the market for more than three decades, to become the world's largest LNG exporter.

Turkish Pipeline

In addition to shipping LNG, Qatar is in the process of constructing a pipeline to transport NG to Europe. In the summer of 2009, Qatar started discussions with Turkey about a pipeline to carry natural gas. This pipeline will traverse Saudi Arabia, Jordan and Syria to arrive to Turkey. Turkey, Bulgaria, Hungary, Austria and Romania are seeking suppliers for a project designed to identify new sources for NG. Plans for the project, named Nabucco, started in 2004, and its aim is to reduce Europe's dependence on Russian gas. In 2014, Nabucco will send as much as 31 billion cubic meters of Caspian and Middle Eastern gas a year via Turkey to Austria.

Production to reach 106 billion m³ of NG in 2010

The largest LNG exporter

Supply NG to Eastern Europe



Increase the LPG production from 4 million tons to 12 million tons per year

LPG

In addition to the huge natural gas development, Qatar is also expanding its LPG production. A byproduct from the refining of crude oil, or extracted from oil or gas streams as they emerge from the ground, LPG is used as a fuel in heating appliances and vehicles, as a refrigerant that does not damage the ozone layer, and mostly as a cooking fuel. LPG was first produced in 1910, and the first commercial products appeared in 1912. Currently, it provides about 3% of the global energy consumed. In 2005, Qatar produced only 4 million tons, but 12 million tons are expected to be produced by 2014.

Building the largest Gas-to-Liquid plant in the world

GTL

Qatar does not only sell its resource in raw form only, it is also in the process of using new technology in order to convert its natural gas into longer-chain hydrocarbons such as gasoline and diesel fuel. This refinery process is called Gas to Liquid (GTL). Qatar Petroleum, in partnership with Shell, is building the Pearl GTL plant in Qatar, set to be the world's largest GTL plant. Its daily production capacity will be around 140,000 barrels of GTL products and 120,000 barrels of associated condensate and liquefied petroleum gas.

Other developments

...and Others

Furthermore, Qatar Petroleum (QP) may replace two natural gas liquid plants (NGL1 and NGL2), built in the late 1980s, by a new smaller plant, because of technological problems. Moreover, QP is considering the economical feasibility of operating two other plants (NGL3 and NGL4).

On the other hand, a new acid gas removal unit, which will be used mainly as a feedstock for petrochemical projects, will be constructed at Mesaieed Industrial City. The plant will produce 21.23 million cubic meters of gas per day.

Good links with regional & international communities

Soft but Smart Politics

Qatar does not only have the gas, which is expected to last 240 years at 2010 projected production levels, it also has the contracts. Long-term contracts to deliver most of the LNG produced by Qatar have already been signed (Appendix A). Although it does not have the largest reserve, Qatar alone has about 25% of the current signed contracts to export LNG, the biggest share. Even though this is partly due to the need of the countries to import natural gas, it is also the result of the soft, but smart politics of Qatar.

Qatar has managed to set up good links with the regional and international communities, which are needed for a commodity exporter. Russia, Iran and Qatar have the biggest natural gas reserves, and together account for more than 53% of the world reserve. On the other hand, the US is the largest natural gas consumer, with more than 21% of the global share. Qatar's politics has reflected positively on the Qatari economy, including the LNG sector. For example, long-term LNG contracts of more than 32 million tons per year were signed with the US. In addition, Qatar has contracts with both China and its small enemy Taiwan. Lately, a new contract to deliver 1 million tons of LNG was signed with Poland. This opens the door of the Eastern European markets for Qatar's LNG.

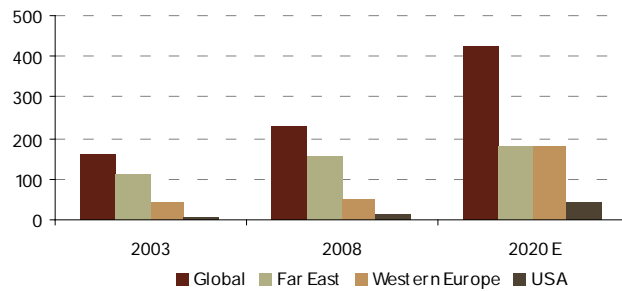
In contrast to most other countries, Qatar does not export natural gas using pipelines. It uses specially constructed vessels instead.



Global Trade

In 1964, United Kingdom imported LNG from Algeria, which became the site of the first commercial LNG plant. Presently, 21 countries are importing LNG.

Chart 5: LNG Imports



Sources: BP and Ocean Shipping Consultant

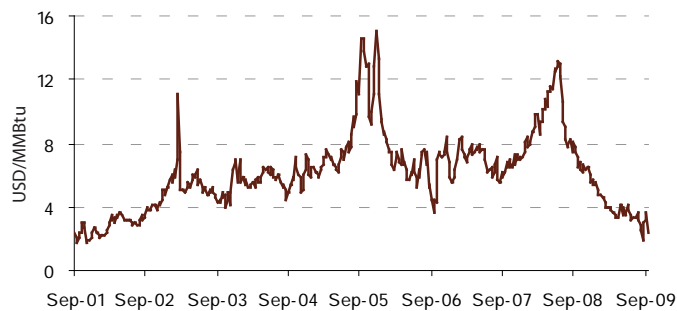
Essentially, LNG trade is showing an upward trend due to two main reasons. First, LNG stake in the NG trade is increasing. LNG accounted for 7.5% of gas supply in 2008, but it is expected to account for 15% in 2015, since new gas exploration projects are located in countries where liquefying NG and shipping it is more feasible as a means of transportation. Second, natural gas demand is expected to increase in the long term.

Natural Gas Demand

The NG demand has been negatively affected by the economic crisis. Consumption of fossil fuel, including NG, declined as industrial production decreased combined with better than expected weather conditions and lower electric power demand. This decrease in demand, accompanied with higher than average storage levels, resulted in dropping of natural gas prices, reflected by the Henry Hub Index, in mid September 2009 to their lowest levels since 2002.

The current economic crisis negatively affects the NG demand

Chart 6: Henry Hub Index



Source: Bloomberg



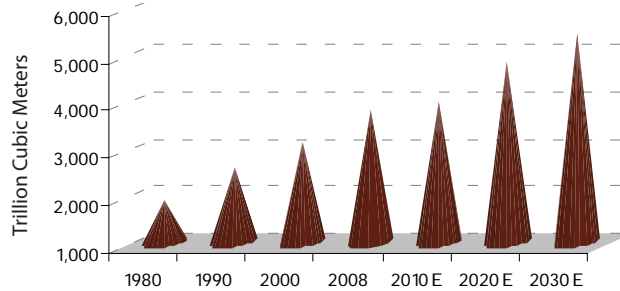
Actually, Qatar can tolerate low NG prices more than any other country, because Qatari plants do not only produce LNG, but also they produce condensate, light oil. Assuming oil prices of USD 68 per barrel, if NG prices reached zero, Qatari gas plants will breakeven. If NG prices reached USD 2 per million Btu, the plants will generate a 12% rate of return, including all expenses.

... but the global demand will restore by 2011

In the coming months, it is expected that the NG demand will restore its high growth phase, especially that most of the biggest global economies will recover. NG prices had showed a rapid increase in the last weeks to break the level of USD 4 per MMBtu. This increase is expected to continue, especially that NG futures are sold at a premium above the spot prices. December 2010 futures, for example, are sold at a premium of 68%.

In fact, natural gas demand is following an upward trend for many reasons. First, natural gas is the cleanest fossil fuel, producing less carbon dioxide per joule delivered than either coal or oil. Cars using natural gas, for example, emit up to 20% less greenhouse gases than gasoline or diesel cars. Second, natural gas can be processed and used for different purposes, including power generation, transportation fuel, fertilizer, manufacturing and others. More than 62% of homes in the world, for instance, use natural gas to fuel stoves, furnaces, water heaters and other household appliances. In addition, when used to generate power, gas-fuelled power plants have lower capital cost, are built faster and work more efficiently than crude oil plants. All these factors support the use of natural gas as an alternative source of energy.

Chart 7: Natural Gas Global Demand



Source: International Energy Outlook

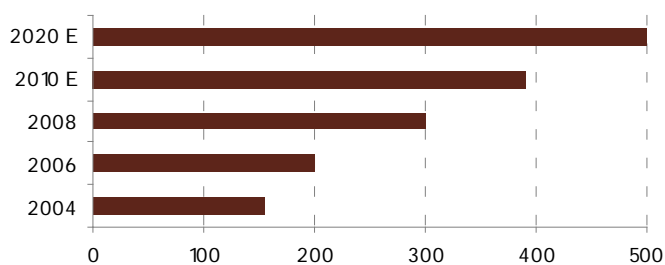


200 LNG vessels are expected to join the global fleet in the coming decade

Global LNG Fleet

Global LNG trade, via ships, started in 1958 when the first commercial LNG cargo vessel crossed the Atlantic from the United States to the United Kingdom.

Chart 8: Global LNG Fleet Size



Sources: Seamanship International and LNG Shipping Solution

Currently, 57 companies in the world are capable of shipping LNG. Some companies operate only one vessel; others operate as many as 36 vessels.

Table 4: Biggest LNG Beneficial Owners

Beneficial Owner	Number of Vessels
Nippon Yusen Kaisha	36
Mitsui OSK Lines	33
Qatar Liquefied Gas	26
MISC Bhd	21
Nigeria LNG	15
Teekay	15
I M Skaugen SE	14
BW Shipping Group	13
Exmar NV	11
Golar LNG	11

Source: Bloomberg

Beneficial owners are those companies that operate the vessels, but do not necessarily own them. They can own the vessels themselves, but also they can rent or charter them.

WHY NAKILAT?

Largest LNG Fleet

Qatar Gas Transport is building the largest LNG fleet in the world. By 2010, Nakilat will own a total of 54 carriers, 25 of which will be wholly owned by the company. Qatar Gas Transport will have a 43% stake in the remaining 29 vessels. In addition, Nakilat has the option to buy two more wholly-owned Q-Max carriers.

Table 5: Nakilat LNG Expected Fleet

		Dec-08	Dec-09	Dec-10
Wholly Owned	Q-Max	4	12	14
	Q-Flex	0	11	11
Joint Venture	Q-Flex	15	20	20
	Conventional	8	9	9
Total		27	52	54

Source: Nakilat website

Upon delivery, Nakilat will have more than 17% of the worldwide LNG fleet, transporting LNG from Qatar to the rest of the world.

Figure 1: Nakilat Shipping Routes



Source: Nakilat Website

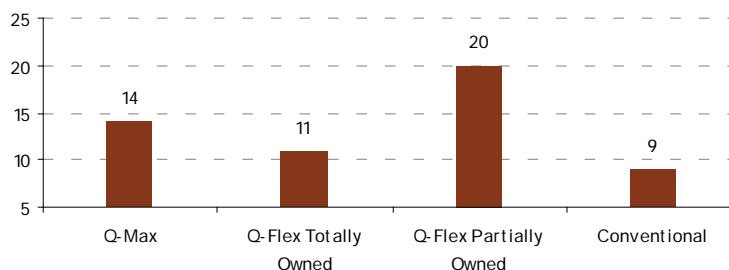
Flexibility

Qatar Gas Transport owns three different types of vessels:

- ☞ Conventional type: each vessel has a capacity of 145,000-154,000 cubic meters.
- ☞ Q-Flex: each ship has 50% more capacity and 40% less energy consumption than the conventional type.
- ☞ Q-Max: each carrier has 80% more capacity and 40% less energy consumption than the conventional type. Q-Max is the largest LNG tanker in the world, and it is produced exclusively for Nakilat.



Chart 9: Fleet by Types, as of March 2010



Source: Nakilat Website

Some ports in the world are not equipped to accept very large vessels such as the Q-Max carrier. Thus, having smaller types of carriers allows Nakilat to deliver gas to such ports.

LPG Expansion

In addition to the LNG fleet, Nakilat has a complementary LPG fleet comprising four very large gas carriers (VLGC), each with a capacity of 82,000 cubic meters. These vessels, which were built at Hyundai Heavy Industries Co. in Korea, are equally owned by Nakilat and Qatar Shipping. In addition, Nakilat plans to add up to 17 LPG ships in order to match Qatar’s increase in the LPG production. In this context, Nakilat has access to nine LPG vessels through a venture signed in January 2008 with the Japanese company Mitsui O.S.K Lines, and it may charter an additional six to eight carriers.

Table 6: Nakilat Expected LPG Fleet

Venture with Qatar Shipping	4
Venture with Mitsui OSK Lines	9
Chartered	8
Total	21

Sources: Nakilat website and Bloomberg

By building this fleet, which is not expected to be completed before 2012, Nakilat will be able to transport about half of Qatar’s LPG output, estimated at 12 million tons per year, by 2014.

And Bulk

In addition to LNG and LPG vessels, Nakilat will expand further into the bulk sector, according to managing director Mohammad Ghannam. Hence, four chartered, bulk carriers will join Nakilat’s fleet, without any further disclosure.

Young and Safe Fleet

After completing its expansion, Nakilat will have the newest fleet in the world. This will be positively reflected in the charter rates. In addition, Nakilat’s shipbuilding contractors are highly experienced Korean shipbuilders with reputable track records, including Samsung, Hyundai and Daewoo.

Acquiring the Needed Experience

Nakilat is a newly established company and has no experience in operating LNG vessels. However, it has entered into a strategic alliance with one of the most experienced companies in operating LNG vessels, Shell International Trading and Shipping Company Ltd. (STASCO).



Secured Revenues

Actually, Nakilat does not have vessels, it has contracted vessels. The company's LNG fleet is chartered on a long-term basis (up to 25 years) from both Qatargas and Rasgas. Both companies have the exclusive right to extract and process the Qatari natural gas.

According to Ghannam, on receipt of delivery notification, it takes less than a minute to forward the vessel to its long-term charter. Hence, Nakilat's revenue stream from wholly-owned vessels is theoretically stable. This could help the company avoid the following troubles:

- ☞ If the Qatar natural gas trains are not completed on time, Qatargas and Rasgas may not use the LNG vessels, but Nakilat will still receive its revenues. In fact, Nakilat is acting as a rental company. It purchases the vessels and then it rents them out.

- ☞ Fluctuation of the spot rates. There is no set market for the LNG shipping rates which depend on two main factors, distance and time, in addition to the change in the quantity supplied. Yet chartering the vessels will theoretically eliminate this risk, because the company will thereby fix its rates and hence secure its revenues.

As a result, Nakilat's utilization rate and revenue stream are expected to be slightly affected by the daily market changes.

Ship Repair Yard

In addition to transporting LNG and LPG, Nakilat has entered into a project to construct and maintain ships and offshore structures in Ras Laffan Port, located in the northeast of Qatar. In 2007, Nakilat and Qatar Petroleum finalized the definition of the project, which is divided into five phases:

- ☞ Phase 1: Repair and conversion of very large ships.
- ☞ Phase 2: Repair of medium-sized ships (20,000 to 80,000 dead weight tons)
- ☞ Phase 3: Fabrication and maintenance of offshore structures and components for land-based petrochemical plants.
- ☞ Phase 4: Construction of high-value, small ships.
- ☞ Phase 5: Repair of small ships.

In March 2007, Nakilat formed a Joint Venture with Keppel Offshore & Marine to operate the new yard. The joint venture will share all the risks and rewards. In addition, a new venture with Damen Shipyards Group BN is expected to be finalized by the end of this year. This venture will be responsible for building marine vessels, with the construction of the first vessel expected to start in mid-2010.

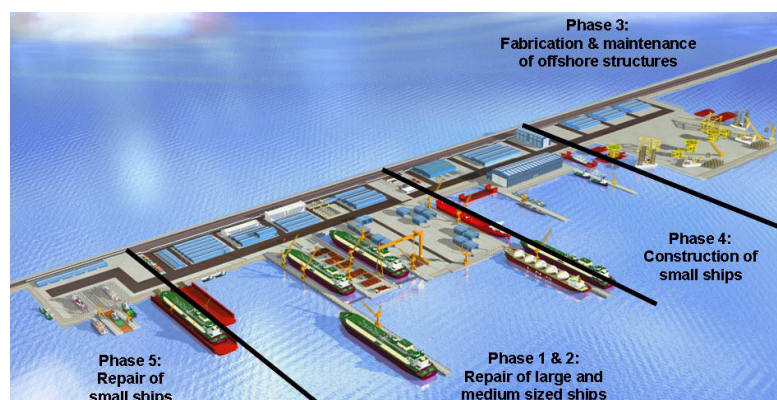
Table 7: Ship Repair Yard Key Features:

Site Area	43 hectares
Dry Docks	One dock 400m long x 80m wide One dock 360m long x 66m wide Both with 12m of water over the sill
Floating Dock	One floating dock 230m long x 38m wide, and 20,000t lift capacity
Quays	Six full length berths, totaling 2.4 kms in length
Workshops	Full range of support facilities
Others	Offices, medical center, fire station, etc.

Source: Nakilat

The new facility, which is being designed in accordance with best international practices, will mainly serve the Nakilat fleet, but it will also undertake work for other ship owners on a commercial basis. The project will be managed by a Project Task Force, with team members from Nakilat, Keppel and Qatar Petroleum.

Figure 2: Ship Repair Yard



Source: Nakilat

Financing the Growth

Being a newly established company with no cash reserves, Nakilat had no other option than getting external loans in order to finance its expansion. In 2006, Nakilat set up its financing program, which was divided into two parts, initial and additional. The company raised USD 4.3 billion of debt (the Initial Program Debt), in December 2006. The Initial Program Debt was well received by the market and was awarded from Euro Money and Marine Money International. In August 2008, Nakilat raised USD 1.5 billion of debt (a part of the Additional Program Debt), and in June 2009, the company raised the final USD 0.95 billion from a group of 17 international and regional banks, despite the deep financial crisis. Therefore, Nakilat secured the needed funds to finish its expansion plans.

Predictable Cost

Nakilat took variable rate loans, at a time where it has stable revenues from its chartered fleet. In order to match the two, Nakilat has entered into an interest rate Swap allowing it to transfer part of its loans to fixed rate. By doing this, the company is trying to match its revenues with its costs and thereby decrease its risk.

Qatar Navigation-Qatar Shipping Merger

Two major shareholders of Nakilat, Qatar Navigation and Qatar Shipping, are expected to merge in the coming few months. When the merger is completed, the newly formed company will be the largest shareholder of Nakilat with a 30% stake. Considering the stakes of other holders, this company may exert a controlling influence over Nakilat, especially for major decisions such as dividend distribution, raising capital, and mergers and acquisitions. However, taking into account the solid relations among Qatar Petroleum, Qatar Navigation and Qatar Shipping, and the vertical relation with the government, we do not expect any major change from the current situation.



As Gas as Stock

Liquidity is not only the feature of the gas that the company transports; it is also the trait of its stock. Nakilat's stock is the one of the most liquid on the Doha Stock Exchange, with QAR 11 billion in value of shares traded during the last 12 months, representing 10% of the total value traded in Qatar during the same period.

Table 8: Top five Liquid Stocks in Doha Stock Exchange during Last 12 Months

	Value Traded (QAR billion)	Percentage of Total Value
Industries Qatar	15	13%
Masref Al Rayan	12	11%
Nakilat	11	10%
Barwa Real Estate	11	10%
Qatar Islamic Bank	10	9%
Doha Stock Exchange	108	100%

Sources: Bloomberg and Audi Capital - KSA

Being a very liquid stock, Nakilat gives investors many advantages over other Qatari stocks, including lower indirect transaction costs resulting in higher net profit, and more price continuity resulting in lower risk.

COMPANY RISKS

As things become clearer, the stock price will move toward its fair value

Clarity is Still Lacking

Even though Nakilat said that its wholly-owned fleet is long-term chartered, it does not disclose chartering prices or conditions. It is not clear, for example, whether the charters pay the fuel cost all the time, or only when the vessel is on hire. Additional costs may thus be charged to Nakilat and so its profitability will depend on the utilization rate. Lower utilization results in higher additional cost and therefore lower profitability.

Because of this ambiguity, we suppose that an additional risk was faced by the investors. As things become clearer, we believe that this temporary risk will decrease, allowing the stock price to move toward its fair value.

Counterparty Risk

Nakilat's fleet is chartered to only two gas companies located inside Qatar, Qatargas and Rasgas. Therefore, Nakilat will face any major risks faced by these companies, in addition to the country risk. If any of these companies faces operating or financial problems and goes bankrupt, Nakilat will receive back its fleet (this what happened with Gulf Navigation Holding in Dubai, in late 2008, when its Probo vessels chartered to Atlas Shipping were called back because of the Atlas' difficult position). However, no such risk is expected to occur as long as gas is pumped in Qatar and imported by outside markets.

Double-Edged Sword

Nakilat's LNG vessels are long-term chartered. This will guarantee a stable revenue stream, but the revenues level could be suboptimal for several reasons.

☞ If the contracts were signed during a down market period, so their terms might reflect adverse market conditions.

☞ Low risk is always accompanied by low return. Because Nakilat will have a rather stable return on its vessels, it has to receive lower revenues than predicted by the market, considering everything else is constant.

☞ The market had reached bottom and the economic environment is showing some signs of improvement. Spot rates will follow the broad market. However, being long-term chartered, Nakilat's carriers will not benefit from such an increase when it happens. On the other hand, operating expenses, not including depreciation, will vary in line with the market. This will result in unstable profitability margins.

Absence of Track Record

Out of its 56 expected LNG vessels in 2010, Nakilat will own 16 Q-Max vessels, a new type of LNG ships that is produced exclusively to Nakilat. This type, even though is expected to be more efficient than the conventional type, is still new and not tried before. The absence of track record for Q-Max will increase the risk for this type, especially in the first year of usage.

Reliquefaction

The greatest risk is posed by possible malfunctions at the reliquefaction plants, which have been experienced by several large LNG shipping companies. To be shipped, natural gas is liquefied at a temperature of -163°C , which requires special and sophisticated technologies. This is done by reliquefaction plants. So far, Nakilat has not encountered such problems, according to the company's charters and partners, but the fear remains.



Troubles in the LPG Sector

The LPG fleet is affected by the current market conditions and so it is expected to have operating difficulties in the short term, which will be reflected negatively on the overall company's revenues.

Interest Rate Risk

Movements in interest rates have two opposite effects on Nakilat:

- ✎ Rising rates will increase the interest expenses the company paid on the portion of the loans not hedged through interest rate Swap agreements.
- ✎ Declining rates will negatively affect the interest revenues the company receives from banks accounts and loans to Joint Ventures.

Market Risk

Qatar Gas Transport had a QAR 101 million Available for Sale portfolio as of June 30, 2009. Even though this portfolio represents a negligible portion of the company's assets, it has a greater effect on the income statement, as they will be marked-to-market on a quarterly basis.



SWOT ANALYSIS

STRENGTHS

- 📁 Building the largest LNG fleet in the world
- 📁 Different vessel sizes assure flexibility
- 📁 Young and safe fleet
- 📁 Stable and secured revenues
- 📁 Complementary projects

WEAKNESSES

- 📁 Lack of transparency
- 📁 Opportunity cost: lower risk, lower return
- 📁 Ambiguity in the LPG sector
- 📁 Operational risks
- 📁 Financing risks

OPPORTUNITIES

- 📁 Expanding in complementary businesses (LPG and cargo)
- 📁 Investing in supplementary projects (the ship yard)
- 📁 May transport petrochemicals (produced by the GTL plant)

THREATS

- 📁 Fear of malfunction in the reliquefaction system
- 📁 Counterparty risk on the interest rate Swap
- 📁 Political instability threatens navigation in the Arabian Gulf



FINANCIAL ANALYSIS

With its solid foundations, Nakilat can look forward to a brilliant future, yet till now it has no history. The company's LNG fleet started partial operations in the last few months, even though the company was founded five years ago. For this reason, past financials, especially income statements, do not reflect the current situation and are expected to be totally changed in the coming quarters.

Table 9: Balance Sheet Analysis

	2007		2008		H1 09	
	QAR million	% change	QAR million	% change	QAR million	% change
Cash & Bank Balance	2,475	-42%	1,990	-20%	1,581	-21%
Trade & Other Receivable	96	67%	134	39%	128	-4%
Current Assets	2,571	-41%	2,127	-17%	1,711	-20%
Construction in Progress	9,382	158%	17,664	88%	9,273	-48%
Fixed Assets	1	226%	2,284	170894%	14,820	549%
Non Current Assets	13,518	111%	22,350	65%	27,370	22%
Total Assets	16,089	49%	24,478	52%	29,081	19%
Current Portion of Debt	-	NA	115	NA	230	100%
Current Liabilities	191	-90%	343	79%	362	6%
Non Current Debt	10,077	70%	19,117	90%	23,114	21%
Fair Value of Interest Rate Swap	1,022	114%	5,016	391%	2,591	-48%
Non Current Liabilities	11,101	73%	24,136	117%	25,710	7%
Total Liabilities	11,292	36%	24,478	117%	26,071	7%
Retained Earnings	201	136%	252	25%	485	93%
Shareholders Equity	5,875	101%	5,910	1%	6,148	4%
Hedging Reserve	(1,082)	127%	(5,915)	446%	(3,143)	-47%

Source: Company Financials

☞ Cash balance is declining because Nakilat has to pay for the vessels it is receiving, on top of the premium paid when the vessels are ordered.

☞ Vessels were recorded on the balance sheet for the first time in Q4 08. This results in an enormous increase in fixed assets in 2008.

☞ In H1 09, the company received 12 wholly-owned vessels. This results in a decrease in the Construction in Progress account and an increase in fixed assets.

☞ The company has debt of QAR 23.3 billion. Interest expenses are partly hedged through the interest rate Swap. The fair value of the Swap depends on interest rate levels, and therefore shows some volatility. The Hedging Reserve represents the group share of the effective portion of changes in the fair value of the Swap. This account, which is expected to decrease with time as the notional amount decreases, is an accounting entry and will not affect the income statement nor the retained earnings.

☞ As the company records more revenues from operations, net income is expected to increase, and so are the retained earnings.


Table 10: Income Statement Analysis

	2007		2008		H1 09	
	QAR million	% change	QAR million	% change	QAR million	% change
Revenues	165	145%	287	74%	654	481%
Depreciation	(0)	52%	(8)	3333%	(103)	47814%
Total Expenses	(35)	59%	(73)	106%	(451)	1959%
Operating Income	130	186%	214	65%	203	124%
Net Income	130	186%	130	0%	234	157%

Source: Company Financials

The first wholly-owned vessel was received in September 2008, and so revenues from wholly-owned vessels were recorded starting in Q4 08, despite the fact that they only constituted a small share of revenue (QAR 25 million). In 2007 and 2008, interest revenues constituted a major part of the total revenues of the firm, as the company was in the pre-operation phase. However, we expect that operating revenues will gradually increase starting from Q2 09, when the company recorded the cost of wholly-owned vessels for the first time. For this reason, a more accurate picture of the financial situation of the company can be obtained by comparing the results of the last two quarters on a quarterly basis.

Table 11: 2009 Income Statement Analysis

	Q1 09		Q2 09	
	QAR million	% change	QAR million	% change
Revenues from Wholly Owned Vessels	106	332%	392	268%
Total Revenues	184	92%	470	155%
Depreciation	(2)	-78%	(102)	5670%
Interest Expenses	(80)	476%	(180)	126%
Total Expenses	(95)	137%	(357)	276%
Operating Income	89	59%	114	27%
Net Income	54	NA	179	229%

Source: Company Financials

☞ Gulf LPG Transport Company, the LPG joint venture between Nakilat and Qatar Shipping, was affected by negative market conditions in H1 09 and made net losses. This adversely affected the company's total revenues.

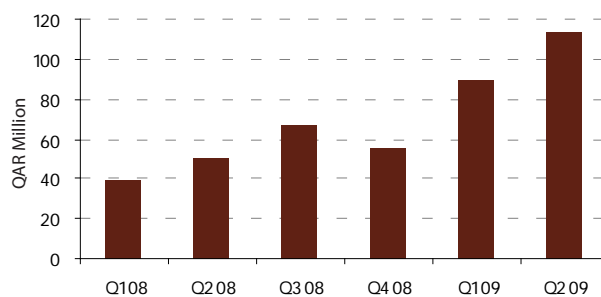
☞ Depreciation expenses showed a supernormal increase in Q2 09 as some vessels started operations in this quarter.

☞ New loans of about QAR 3.5 billion were taken in H1 09, which was reflected in an increase in interest expenses.

☞ The supernormal growth stage is expected to last four more quarters as new LNG vessels will be received and chartered out.



Chart 10: Quarterly Operating Income



Source: Company Financials

VALUATION

Since Nakilat operated only a few vessels in the second quarter of the year, past revenues represented a small portion of the total expected revenues. We expect that operating revenues will increase gradually in the coming quarters for two main reasons:

- ☞ New capacity will be added, but more important,
- ☞ Nakilat chartered vessels contracted with Qatargas and Rasgas will be totally operated by 2010.

Due to the lack of transparency from the company, especially on the revenues decomposition and future expansion plans, some of our assumptions were based on data released by global companies involved in the LNG shipping sectors. These data were adjusted to better reflect the case of Nakilat:

- ☞ The LNG shipping rates are positively related to the distance of the destination. Most of the Nakilat shipments are to UK and USA, which are long distances. This will positively affect the rates.
- ☞ There are different types of the LNG carriers. Each type has its own rate that mainly depends on its supply and demand. Q-Max ships are only produced to Nakilat and so they were priced according to specialized contracts. We expect that the contracts will consider the characteristics of these carriers including the capacity and the fuel consumption.

In addition we were conservative, but realistic, in making the following assumptions:

- ☞ Even though it takes less than a minute to forward the vessel to the charters, as mentioned by the company, we believe that totally owned vessels delivered in 2009 will wait for 90 days before they start operations.
- ☞ Nakilat has entered into a Swap agreement in order to try to fix the interest payments. The fair value of the interest Swap and the hedging reserve will change as the market interest rates change. Going forward, Nakilat will benefit from an increase in the interest rates. The fair value of the Swap will improve, reducing the company's liability. The hedging reserve, an account which is recorded against the company's equity, will also decrease.

Based on these assumptions, two valuation methods were conducted to obtain the company's fair value. Each valuation was based on a three stage model:

- ☞ In the first stage, the company will receive its ordered 58 vessels according to a specific schedule, and so yearly financials were forecasted.
- ☞ In the second stage, we assume that the company will continue its LPG and bulk growth. This stage is expected to last two years. A growth of 14% and 12% is expected in the first and second year, respectively.
- ☞ Finally, a terminal growth rate of 2% was assumed.



Free Cash Flow (FCF) Model

We have conducted a FCF valuation for Qatar Gas Transport Company in order to obtain our fair value. A weighted average cost of capital (WACC) of 6.71% was used, and a fair value of QAR 48.08 was obtained, indicating a 90% upside potential over the current price of QAR 25.30.

Table 12: Free Cash Flow Model

	2009 E	2010 E	2011 E
Net Income QAR million	571	1,395	1,428
Non-Cash Charges QAR million	417	679	685
After Tax Interest Expense QAR million	663	896	904
Capex QAR million	22,809	1,805	237
Change in Working Capital QAR million	210	115	4
Free Cash Flow to the Firm QAR million	-21,368	1,049	2,776
Present Value of Free Cash Flow to the Firm QAR million	-21,368	984	2,443
Present Value of Terminal Value QAR million			60,975
Intrinsic Value of the Firm QAR million			48,385
Net Debt QAR million			21,763
Intrinsic Value of Equity QAR million			26,623
WACC			6.59%
Terminal Growth Rate			2.0%
Shares Outstanding (million)			553.67
Fair Value (QAR)			48.08

Source: Audi Capital - KSA Estimates

Dividend Discount Model (DDM)

Although it has not paid dividends so far, we assume that Nakilat's financial position will allow it to start paying dividends in 2011. At that time, Nakilat will finish its supernormal growth phase, especially that related to LNG, and it will generate a positive free cash flow to equity. As a result, we assume that the company could afford an 85% payout ratio. Under this assumption, we have conducted a DDM valuation for Nakilat. A cost of equity of 10% was used and a fair value of QAR 29.42 was obtained, indicating an upside potential of 16% from the current price of QAR 25.30.

Table 13: Dividend Discount Model

	2009 E	2010 E	2011 E
Net Income (QAR million)	571	1,395	1,428
Number of Shares Outstanding (million)			553.67
Earnings per Share (QAR)	1.03	2.51	2.57
Dividends per Share (QAR)	0.00	0.00	1.93
Present Value of Dividends per Share (QAR)	0.00	0.00	1.59
Present Value of Terminal Value (QAR)			29.37
Cost of Equity			10.00%
Terminal Growth Rate			2.00%
Fair Value (QAR)			29.42

Source: Audi Capital - KSA Estimates



We assigned an 80% weight to the FCF model and 20% to the DDM. As a result, a fair value of QAR 44.35 was derived, indicating an upside potential of 75% from the current price of QAR 25.30.

Table 14: Fair Value

	Price (QAR)	Weight	Price Contribution
FCF	48.08	0.80	38.47
DDM	29.42	0.20	5.88
Fair Value (QAR)	44.35		

Source: Audi Capital - KSA Estimates

It is worth to note that comparative valuation is not considered because such valuation may be misleading for Nakilat for the following reasons:

- ☞ The company's revenues breakdown are special in nature in that the company's LNG fleet is long term chartered, whereas most other companies charter their vessels on a short term basis.
- ☞ Nakilat is a high growth company that has no comparable peers either in the region or in the world.
- ☞ By 2010, Nakilat will have 54 LNG vessels out of a total 58 vessels, representing more than 93% of the total fleet. The LNG sector in most of other companies represents a much lower percentage (<40%). Thus the revenues of these companies are not affected by the LNG sector only. As a result, it is meaningless to compare Nakilat to these companies.



PRO FORMA FINANCIALS

Table 15: Balance Sheet

QAR million	2006	2007	2008	2009 E	2010 E	2011 E
Cash & Equivalents	4,299	2,475	1,990	948	236	688
Receivables	58	96	134	298	506	513
Due from Joint Ventures	19	0	3	2	3	4
Inventories	0	0	0	1	1	1
Total Current Assets	4,376	2,571	2,127	1,249	746	1,206
Loans to Joint Venture Companies	497	1,547	588	882	794	675
Investment in Joint Ventures	2,193	2,457	1,464	1,947	2,141	2,248
Available for Sale	73	130	97	121	145	174
Construction in Progress	3,635	9,382	17,664	1,791	910	115
Net PP&E	0	1	2,284	24,475	26,235	26,466
Deferred Financing Cost	-	-	253	280	300	350
Total Non Current Assets	6,398	13,518	22,350	29,496	30,525	30,028
Total Assets	10,773	16,089	24,478	30,745	31,271	31,234
Borrowings	-	-	115	368	354	361
Payables	101	191	228	177	270	274
Due to Related Party	1,821	0	0	5	5	5
Total Current Liabilities	1,922	191	343	550	629	641
Borrowings	5,925	10,077	19,117	24,188	23,221	22,231
Fair Value of Interest Swap	478	1,022	5,016	1,958	988	521
Provision for End of Service Benefits	1	2	3	5	6	7
Total Non Current Liabilities	6,404	11,101	24,136	26,151	24,215	22,759
Equity Attributed to Equity Holders of the Parent	2,922	5,875	5,910	6,550	7,955	8,328
Hedging Reserve	(477)	(1,082)	(5,915)	(2,512)	(1,534)	(500)
Minority Interest	3	4	4	5	6	7
Total Equity	2,448	4,796	(1)	4,043	6,427	7,835
Total Liabilities and Equity	10,773	16,089	24,478	30,745	31,271	31,234

Sources: Company Financials and Audi Capital - KSA Estimates


Table 16: Income Statement

QAR million	2006	2007	2008	2009 E	2010 E	2011 E
Revenues	68	165	287	1,989	3,612	3,664
Depreciation	(0)	(0)	(8)	(409)	(673)	(679)
Interest Expenses	0	0	(14)	(710)	(896)	(904)
Total Expenses	(22)	(35)	(73)	(1,418)	(2,247)	(2,276)
Operating Income	45	130	214	571	1,365	1,388
Others	0	0	(84)	1	30	40
Net Income	45	130	130	572	1,395	1,428
EPS QAR	0.08	0.23	0.23	1.03	2.51	2.57

Sources: Company Financials and Audi Capital - KSA Estimates

Table 17: Ratios

	2006	2007	2008	2009 E	2010 E	2011 E
<i>Liquidity Ratios</i>						
Current Ratio	2.28	13.45	6.21	2.27	1.19	1.88
Quick Ratio	2.28	13.45	6.21	2.27	1.18	1.88
Cash Ratio	2.24	12.95	5.81	1.72	0.38	1.07
<i>Solvency Ratios</i>						
Interest Coverage Ratio	NA	NA	NA	1.96	2.52	2.54
Financial Leverage	3.69	2.74	4.14	4.69	3.93	3.75
Non Current Assets to Equity	2.19	2.30	3.78	4.50	3.84	3.61
Debt to Equity	2.03	1.72	3.25	3.75	2.96	2.71
<i>Turnover Ratios</i>						
Total Assets Turnover	0.01	0.01	0.01	0.07	0.12	0.12
Fixed Assets Turnover	164.81	189.26	0.25	0.15	0.14	0.14
<i>Profitability Ratios</i>						
Operating Profit Margin	67%	79%	75%	29%	38%	38%
ROE	2%	3%	2%	9%	27%	20%
ROA	0%	1%	1%	2%	4%	5%

Source: Company Financials and Audi Capital- KSA Estimates



APPENDIX

Table 18: Qatari Contracts to Export LNG

Export Venture	Importer	Start Year	End Year	Volume million tons/year
Qatargas	Poland	2014	2034	1.00
Qatargas 4	China	2012	2026	3.00
Qatargas 3	Thailand	2011	2021	1.00
Qatargas 4	USA	2011	2036	7.80
Shell Portfolio	Dubai	2010	2025	1.50
Qatargas 3	USA	2010	2035	7.80
Qatargas2	China	2009	2023	2.00
Qatargas3	France	2009	2034	1.85
Rasgas 2	India	2009	2030	2.50
Rasgas 3	Kuwait	2009	2013	1.60
Qatargas 2	Mexico	2009	2034	0.70
Qatargas 2	USA	2009	2034	1.20
Qatargas 2	UK	2009	2034	1.50
Qatargas 2	Japan	2008	2013	1.20
Rasgas 2	Taiwan	2008	2033	3.00
Rasgas 3	USA	2008	2033	15.60
Qatargas 2	UK	2008	2033	10.40
Rasgas 2	Belgium	2007	2011	3.40
Rasgas 2	Belgium	2007	2027	2.05
Rasgas 2	Italy	2007	2030	4.70
Rasgas 3	South Korea	2007	2027	2.10
Qatargas 1	Spain	2006	2025	0.75
Qatargas 1	Spain	2005	2025	0.75
Rasgas 2	Spain	2005	2025	0.80
Rasgas 2	India	2004	2028	5.00
Rasgas 2	Spain	2004	2022	0.75
Qatargas 1	Spain	2002	2012	0.66
Qatargas 1	Spain	2001	2012	0.66
Rasgas 1	South Korea	1999	2024	4.80
Qatargas 1	Japan	1998	2021	0.20
Qatargas 1	Japan	1998	2021	0.52
Qatargas 1	Japan	1998	2021	0.29
Qatargas 1	Japan	1998	2021	0.12
Qatargas 1	Japan	1998	2021	0.35
Qatargas 1	Japan	1998	2021	0.35
Qatargas 1	Japan	1998	2021	0.17
Qatargas 1	Japan	1998	2021	4.00

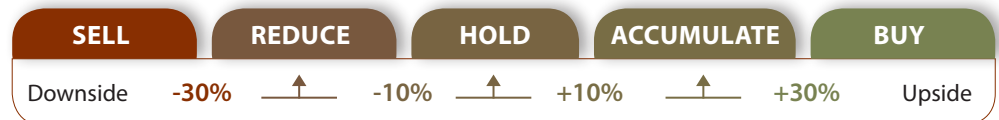
Source: Bloomberg



FAIR VALUE DEFINITION

It is an unbiased estimate of the 12-month potential market price of the stock

RECOMMENDATION GUIDE



BUY: Upside potential in share price is more than 30%

ACCUMULATE: Upside potential in share price is between 10 and 30%

HOLD: Upside or downside potential in share price less than 10%

REDUCE: Downside potential in share price is between 10 and 30%

SELL: Downside potential in share price is more than 30%

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