Renaissance Capital

Initiation of coverage
BUY
TP: EGP4.55
Industrials
Egypt

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Qalaa Holdings
The macro guys

We initiate coverage of Qalaa Holdings (QH) with a BUY rating and a TP of EGP4.55. QH is an Egyptian macro-driven investment company that offers broad investment exposure to the theme of energy reform in Egypt. Its assets are currently under-valued, in our view, as the full impact of these reforms is yet to be reflected in their financial performance.

QH is an under-valued investment company

QH owns 10 core companies that are grouped into energy, cement, logistics & transportation, mining and agri-foods. It also owns nine companies in non-core sectors, which are legacy assets from its former incarnation as a private equity firm, and which it aims to divest in the medium term. Around 80% of the investment exposure is in Egypt, with the balance in Sudan, Kenya, Uganda and Algeria. We believe the market is currently assigning value only to Asec, Egyptian Refinery Company (ERC) and Taqa Arabia, and zero to the rest.

Diverse sectors, one over-riding theme – energy reforms

We believe QH's gearing to the theme of energy reforms is difficult to replicate. Primary beneficiaries, in our view, include its power and gas asset (Taqa Arabia), its integrated waste management company (Tawazon), its river transport platform (Nile Logistics) and its upcoming fuel bunkering facility (Mashreq). Indirect beneficiaries include its largest asset, Asec Holding, as we believe cement margins are set to rise on feedstock changes, while ERC, its greenfield refinery, is an import substitution play of national significance that is set to thrive on Egypt's need for refined products.

Asset sales and volume growth are key catalysts

Having transformed into an investment company, QH has announced a detailed asset disposal plan for the near term, which we believe will be positive for the stock on sentiment and reduce leverage. The underlying financial performance of its companies will also improve substantially, in our view: we expect EBITDA to grow c. 10x by 2017E.

TP implies 44% upside potential; risks are regulatory and execution

We forecast company-specific earnings for ERC, Taqa Arabia, Asec Cement, Nile Logistics, Africa Railways and Tawazon and use industry benchmarks (EV/EBITDA, P/E) for our valuations; the rest we take at investment cost or at market value. We derive c. 75% of our total fair value from our bottom-up forecasts. Our SoTP-derived TP of EGP4.55 implies 44% upside potential vs current levels. Key risks are regulatory, given the large exposure to downstream energy, and execution on greenfield and add-on projects.

Report date:	29 January 2015
Current price, EGP	3.17
Upside/downside, %	44
MktCap, EGPmn	5,804
Average daily volume, EGPmn	30
Free float	33.97%
Bloomberg	CCAP EY

Prices in this report are as of market close on 27 January 2015.

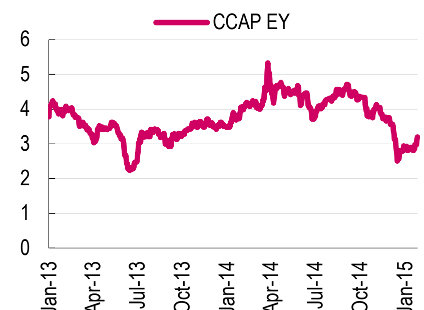
Summary valuation and financials, EGPmn (unless otherwise stated)

	2010	2011	2012	2013
Operating income	-1,268.1	-414.5	-313.4	-313.1
Pre-tax income	-1,355.9	-800.5	-701.3	-384.9
Net income	-1,354.9	-773.5	-691.7	-374.7
Total assets	5,002.9	5,040.9	5,774.4	30,039.6
Cash	162.6	166.2	255.2	2,149.9
Net debt	1,089.5	1,186.5	2,211.1	7,765.1
Shareholders' equity	2,556.3	3,057.8	2,289.2	12,723.7
Minorities	197.0	379.7	438.3	8,699.1
EPS, EGP	-2.1	-1.1	-0.8	-0.4

Note: Historical data. Given QH's structure, our valuation incorporates forecasts for core assets only; further details provided elsewhere in this report.

Source: Company data

Figure 1: Price performance – 52 weeks, EGP



Source: Bloomberg

Important disclosures are found at the Disclosures Appendix. Communicated by Renaissance Securities (Cyprus) Limited, regulated by the Cyprus Securities & Exchange Commission, which together with non-US affiliates operates outside of the USA under the brand name of Renaissance Capital.

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Investment summary

QH's key investments are geared to energy

Cutting subsidies means a changing landscape for power, industry and transport

Egypt's initial cut of subsidies, in July 2014, marked the start of a process that we believe will result in fundamental changes in the Egyptian economy. Energy subsidies have not only weighed on state budget for decades, they have also distorted the foundations of industrial production, power generation and transport by rendering them uneconomical. Now the plug has been partially pulled (with a c. 70% price increase in July 2014), we believe the government and the private sector will have to work together to find solutions to the structural problems that the subsidy regime helped to propagate and conceal. In our view, QH should be seen as a proxy for that trend.

We see three key pivots of the economy being affected by higher energy prices, in particular natural gas prices.

1. Power: Natural gas accounts for 84% of the energy used by Egypt's power generation plants, and around two-thirds of Egypt's gas production is used to generate electricity.

2. Industry: Cement, steel and most heavy industry mainly use natural gas as feedstock; where they do not, they use heavy fuels and mazut.

3. Transport: Egypt has chronically underinvested in rail and river transport, in our view, and its roads are notoriously dangerous, as subsidies have made road transport for cargo (and passengers) artificially cheap.

To add to the issue of price rises, we also note basic supply constraints, since Egypt's energy balance (again, in natural gas especially) is exceptionally tight and sometimes in outright deficit. Since the revolution in 2011, Egypt has seen pressure on its state finances, and the Central Bank has had to use a majority of its FX reserves to guarantee stable supplies of energy imports, given the declines in domestic output. The Central Bank has announced that it aims to clear a significant portion of the debt still owed to foreign energy companies, but it will also have to contend with the debts incurred domestically by Egypt's own energy sector. According to the Ministry of Electricity and Energy, power generation companies alone owe the state some $10bn. The significant spillover of a failed energy policy on state finances illustrates the urgency with which Egypt needs to deal with the underlying economics of supply, production, distribution and transport of energy. Our view is that the downside risk of doing nothing more is so great that it could bring down any government, and so should be viewed as a matter of national security. This is why we think the authorities are likely to make energy reform the centrepiece of their domestic economic agenda in the medium-to-long term.

Current and medium-term impact on corporate investments

Higher energy prices will result in three core investment themes, in our view.

1. Feedstock diversification and efficiency drives

Since energy input costs are rising, and set to rise further, energy-intensive industries – in effect most heavy industry – are going to have to prioritise cost-effective alternatives to their historical feedstock. Already the government has moved to allow private sector coal imports, which in our view is bound to result in coal becoming a sizeable part of the country's future energy mix, subject to further legislation and investments. Other energy sources, such as biomass and refuse-derived fuels, are also likely to gain in relative importance, albeit from a low base. We believe companies are likely to invest in maximising energy efficiency, either by the use of new technology or with a greater

emphasis on recycling, heat recovery and so on. All these measures will require new investment.

2. Power generation and distribution

Since input prices are likely to continue rising and output is becoming more market-driven (via falling subsidies), we expect the economics of power generation will gradually improve. We believe the private sector will be strongly encouraged to participate in the sector and we also expect incentives linking direct, bilateral distribution with generation. Egypt's current installed capacity of c. 32,000 MW – as per currently announced public-sector-driven initiatives – is set to rise by over 50% in the near term, in our view.

Since so much of power generation is contingent on natural gas as a feedstock, and given the tight power supply, we think importing more gas will be a key priority. The government has issued tenders for several floating storage and regasification units (FSRU) so that it can import liquefied natural gas (LNG), which will require significant related investments and infrastructure.

As is the case for heavy industry, diversification into more efficient alternatives is also likely to be prioritised and see significant investment. We see solar and wind energy as likely top contenders here.

3. Transport

Rail and river transport are likely to become increasingly competitive vs road and should see substantial investment. The infrastructure required to import large-scale volumes of coal and LNG, and to transport them, will add to the investment required.

We believe QH's companies are major beneficiaries of these trends, not only because of their exposure to the energy sector reform theme, but also because of the catalytic quality that energy reform is having on their financial performance.

We view QH as geared to the energy reform theme in two principal ways: first, because the majority of its portfolio is thematically anchored in that story; and second, because most of its companies' financial performance will benefit strongly from the changes that energy reforms are set to unleash, in our view.

Figure 2: Key beneficiaries of energy reforms in QH's portfolio

Company	How is it linked to energy reforms?	How is its financial performance affected?
Taqa Arabia	Leading private-sector power generation, engineering, procurement and construction, and gas distribution	Strong top-line growth on booming demand
Tawazon	Leading private-sector recycling, biomass, refuse-derived fuels	Strong top-line growth on booming demand
ERC	Largest refinery in Egypt, import substitution, rising demand for its products	Even stronger demand for its products, technology could be replicated
Mashreq	Scheduled to be first of its kind fuel-bunkering facility near the Suez Canal	–
Asec Holding	Margin gains on feedstock changes and energy efficiency	Rising EBITDA margins on efficiency gains
Nile Logistics	Competitive price advantage vs road + coal imports	Viability of business model, volume growth

Source: Renaissance Capital

QH's core portfolio should see strong top-line gains in the coming years, and will be further boosted by ERC in 2017

Based on the companies that we model, the near-term outlook appears favourable to us, with all companies posting strong sales and volume growth, reflected in sharp EBITDA gains in our forecasts.

The numbers in Figure 3 account neither for minority ownership (such as ERC) nor for eliminations, as our intention is to highlight the catalytic nature that we believe energy

reforms are likely to have on the holdings in aggregate. We believe there is potential upside risk to our estimates stemming from companies that we do not include in our forecasts, or that may be disposed of in the forecast period. QH management has guided for consolidated EBITDA figures that are higher, given the difference between the company's aggregate view and our estimates, which include only what we think are the most important assets.

Figure 3: EBITDA outlook, EGPmn

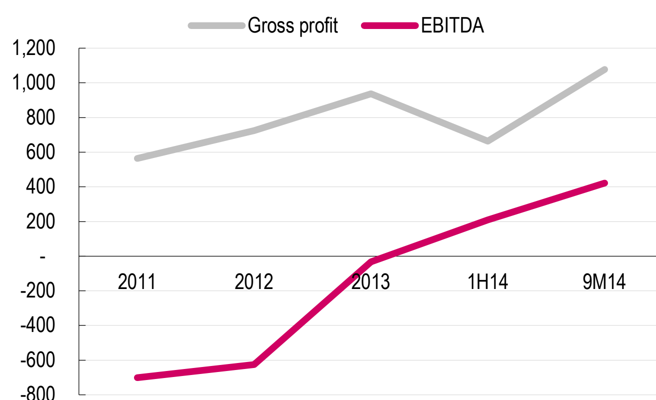
	2013	2014E	2015E	2016E	2017E
CC/SPV	-120				
Asec Holding	84	425	692	741	844
Taqa Arabia	130	155	243	365	577
Tawazon	-16	33	50	122	177
ERC	-22				3,852
Mashreq	-16				
Nile Logistics	-131	-13	32	93	128
Africa Rail	-26	-37	127	256	442
Gozour	150				
Wafra	-17				
Tanmyah	10				
Miscellaneous/non-core	15				
Eliminations	-75				
Total	**-33**	**563**	**1,144**	**1,578**	**6,020**
Total ex. ERC	-33	563	1,144	1,578	2,168

Source: Company data, Renaissance Capital estimates

Key operational metrics at the consolidated level are already showing positive momentum on Egypt's economic recovery and on operational improvements

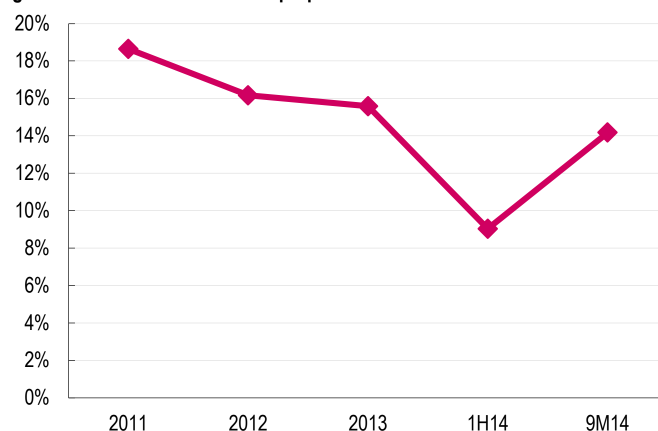
QH's consolidated figures are showing some improving trends in gross profits (sales – CoGS), as well as in EBITDA. Similarly, sales volumes have started to recover following greater political stability and a recovering domestic economy. Taqa Arabia, Asec Cement and Gozour account for most of the improvements, given their comparatively larger size, although in relative terms Tawazon appears to be showing the best growth dynamics.

Figure 4: Consolidated gross profits and EBITDA, EGPmn



Source: Company data

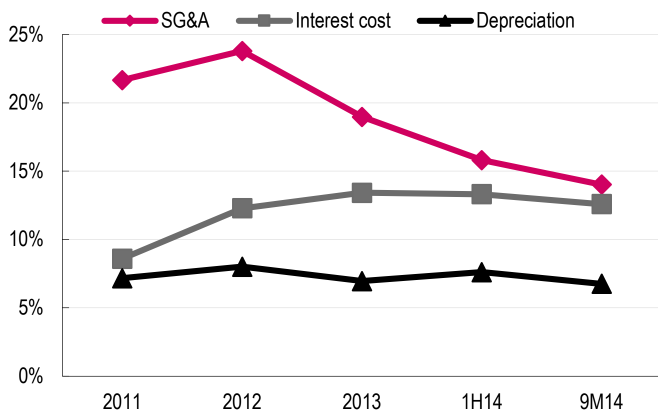
Figure 5: Consolidated sales as a proportion of assets



Source: Company data

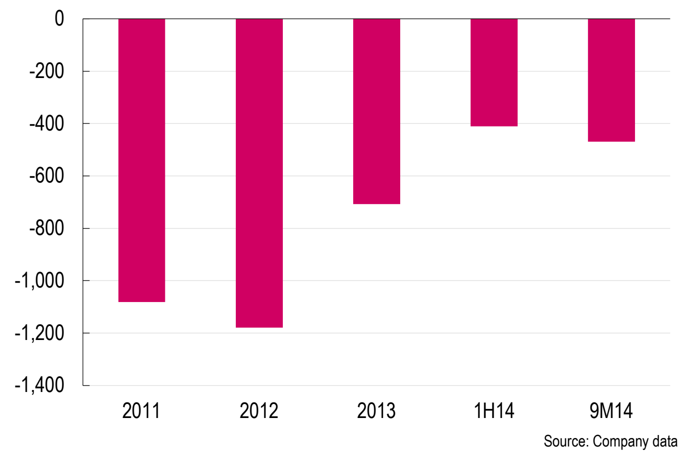
QH's overall expense ratio as a percentage of sales (SG&A/sales) has fallen as a result of growing sales, although the growth rate of SG&A expenses has also slowed significantly in recent quarters. However, interest and depreciation costs remain a significant drag. QH was loss-making as at 9M14, with only Taqa Arabia and Tawazon making profit among the core companies. Outside of these, Tanmeyah (which QH considers long-term non-core) is currently the only other profitable entity.

Figure 6: Key expense items as a proportion of sales



Source: Company data

Figure 7: Consolidated net income (loss), EGPmn



Source: Company data

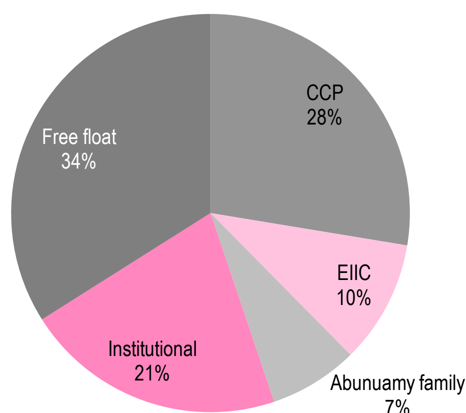
Company description

History and ownership

QH was known until mid-2014 as Citadel Capital. It was founded in 2004 by Ahmed Heikal and Hisham Al Khazindar as a private equity firm. From modest beginnings (paid-in capital was EGP2mn at inception), the firm grew quickly through a series of transformational, high-return transactions that spawned capital to invest further and a reputation for strong deal-making. Between 2004 and 2012, the firm created 19 investment-specific funds, raised and invested equity of c. $4.9bn, including c. $1bn of own equity, and invested in over 15 sectors and countries in 54 transactions (including buyouts, roll-ups, and greenfield and turnaround projects). Citadel Capital grew to become the largest private equity player in Africa, controlling $9.5bn in investments (including debt). The firm changed its name to Qalaa Holdings in 2014, marking its transition from a private equity firm to an investment company.

The firm is controlled via preference shares (3:1 voting rights) by Citadel Capital Partners (CCP), an investment vehicle created by the founders (and now also including some senior executives) specifically to maintain control of the firm. As at FY14, CCP owned 27.6% of the outstanding shares, Emirates International Investment Company (EIIC) owned 10.01%, the Abunumany family owned 7.22%, regional and international investors owned 21.2%. and the balance (33.9%) was free float.

Figure 8: NH – current shareholding structure



Source: Company data

Investments and footprint

QH's main investments (labelled 'core') are in the following segments: energy, cement, agri-foods, transportation & logistics, and mining. Non-core investments are scheduled for sale and operate in more diverse sectors. Geographically, most of the investment exposure is in Egypt, but some investments in cement, agri-food and transportation are in Algeria, Sudan and South Sudan, Ethiopia, Kenya and Uganda.

Figure 9: QH – investments

Company	Segment	% ownership	Year	Brief desciption
Core:				
Taqa	Energy	62.5%	2006	Gas distribution, power EPC & mgmt, fuel marketing
Tazawon	Energy	47.9%	2007	Solid waste management
ERC	Energy	15.2%	2009	Greenfield hydrocracker
Mashreq	Energy	54.9%	2009	Fuel storage & bunkering
Asec Holding	Cement	69.2%	2004	Cement production, engineering, construction & mgmt of plants
Gozour	Agri-foods	43.1%	2007	Dairy farm, food brands, growing super market chain
Wafra	Agri-foods	100.0%	2007	Large lands base w/full irrigation rights, growing cereals & crops
Nile Logistics	Transportation & Logistics	62.0%	2007	River transportation (barges), stevedoring, container handling
Africa Railways	Transportation & Logistics	30.8%	2009	Operates national railway of Kenya and Uganda
Ascom	Mining	39.2%	2006	Various production & export
Non-core:				
Tanmeyah	Microfinance	70.0%	2009	
Finance Unlimited	Financial Services	99.9%	2008	
United Foundries	Metallurgy	64.7%	2009	
Grandview	Mid-cap buyouts	47.6%	2006	
Bonyan	Real Estate	42.8%	2007	
Tanweer	Media & Retail	60.2%	2007	
NPC	Upstream Oil & Gas	15.0%	2005	
NVPL	Upstream Oil & Gas	15.0%	2009	

Source: Company data

As of 9M14, QH had invested around $1bn of own capital.

Figure 10: QH – own investments as at 9M14

Asset	Segment	QH Investment in EGPmn	% of investment cost	Investment cost in $**
Asec Holding*	Cement	1,580,208,574	19%	197,526,072
Taqa Arabia	Energy	608,580,578	7%	76,072,572
ERC	Energy	506,645,635	6%	63,330,704
Mashreq Petroleum	Energy	67,794,210	1%	8,474,276
Tawazon	Energy	52,598,129	1%	6,574,766
Nile logisitcs	Transport & logistics	342,879,721	4%	42,859,965
Africa Railways	Transport & logistics	247,190,798	3%	30,898,850
Gozour	Agri-food	762,234,594	9%	95,279,324
Wafra	Agri-food	186,192,878	2%	23,274,110
ASCOM	Mining	183,114,262	2%	22,889,283
Sub-total		**4,537,439,379**	**54%**	567,179,922
Non-core		2,658,856,148	32%	332,357,018
Assets written off		982,073,639	12%	122,759,205
Others		149,672,570	2%	18,709,071
Total		**8,328,041,735**	**100%**	1,041,005,217

*Inclusive of a convertible shareholders' loan.
**Using an exchange rate of EGP8.0/$.

Source: Company data

Figure 11: QH – assets, equity, debt and cash, EGPmn

	Assets				Equity				Total borrowing				Cash			
	2011	2012	2013	1H14	2011	2012	2013	1H14	2011	2012	2013	1H14	2011	2012	2013	1H14
CC/SPV	5,041	16,991	22,520	3,268	3,058	11,337	15,997	6,592	1,353	2,410	2,918	2,887	166	234	224	258
ERC	5,099	6,727	10,182	10,894	3,440	4,639	6,287	5,381	0	1,536	1,629	3,514	1,386	798	1,081	580
Taqa Arabia	2,734	2,535	2,320	2,345	1,320	1,223	1,118	427	265	234	231	278	102	354	514	554
Tawazon	249	280	218	226	123	153	120	96	48	42	13	14	13	10	1	8
Mashreq	137	144	155	175	96	100	132	27	0	0	0	0	8	8	5	5
Asec	7,211	6,778	7,592	8,092	2,631	1,620	1,603	959	2,006	2,203	2,492	2,429	396	211	126	145
Gozour	2,236	1,972	2,057	2,512	1,136	655	520	235	473	457	614	534	24	42	38	65
Wafra	235	221	246	264	-124	-213	-274	-290	343	57	58	57	3	2	1	15
Nile Logistics	843	850	726	877	491	334	144	-134	277	317	356	374	10	8	3	8
Africa Railways	258	2,055	2,905	2,344	-173	1,221	1,696	313	132	453	831	1,261	29	110	83	455
Tanmeyah	40	50	62	74	-2	1	-3	-23	3	0	0	0	10	8	15	36
Non-core	1,305	1,219	1,087	1,323	487	230	80	-348	323	261	259	234	6	4	6	55
Eliminations	-1,000	-13,360	-19,239	0	1,460	-9,182	-14,064	0	-320	0	-669	0	1	1	1	0
Total	**24,389**	**26,461**	**30,832**	**32,394**	**13,945**	**12,117**	**13,356**	**13,237**	**4,904**	**7,969**	**8,732**	**11,581**	**2,155**	**1,790**	**2,098**	**2,184**

Source: Company data

Figure 12: QH – revenue, gross profits, EBITDA and net income, EGPmn

	Revenue				Gross profit				EBITDA				Net income			
	2011	2012	2013	1H14	2011	2012	2013	1H14	2011	2012	2013	1H14	2011	2012	2013	1H14
CC/SPV	0	0	0	0	0	0	0	0	-754	-143	-120	-98	-774	-178	-134	-138
ERC	0	0	0	0	0	0	0	0	5	-125	-22	-15	17	-102	-31	-13
Taqa Arabia	1,161	1,110	1,262	721	252	233	263	143	134	120	130	65	77	88	56	37
Tawazon	89	116	86	33	13	20	-7	6	3	4	-16	3	-5	-7	-18	0
Mashreq	0	0	0	0	0	0	0	0	-12	-12	-16	-7	-11	-11	-12	-5
Asec	1,701	1,462	1,661	1,204	-18	96	212	295	-315	-101	84	203	-671	-715	-352	-192
Gozour	884	926	1,066	504	274	280	334	150	46	-54	150	69	-279	-456	-131	-59
Wafra	9	7	12	2	3	-16	2	-1	-28	-54	-17	-8	-36	-53	-35	-9
Nile Logistics	63	59	43	26	-10	-17	-15	-6	-71	-56	-131	-17	-84	-81	-153	-42
Africa Railways	434	365	458	323	-36	9	46	23	-84	-60	-26	-15	-119	-148	-145	-105
Tanmeyah	45	65	66	43	45	65	66	43	-22	7	10	17	-25	2	5	15
Non-core	160	169	152	70	41	55	34	12	17	-33	15	-21	-119	-234	-150	-100
Eliminations	0	0	0	0	0	0	0	0	380	-119	-75	34	947	716	392	201
Total	**4,547**	**4,279**	**4,806**	**2,928**	**565**	**724**	**936**	**664**	**-701**	**-626**	**-33**	**210**	**-1,081**	**-1,180**	**-708**	**-411**

Source: Company data

The macro view underlying the investments

QH's founders have structured their investments around a thoroughly macro-driven view of Egypt's economy and its place within the region and beyond. The core themes can be summarised as follows.

- Egypt's subsidies of energy and commodities are unsustainable.
- The eventual removal of those subsidies will create market dislocations requiring far higher levels of private-sector investment, implying a higher degree of market liberalisation.
- A gradual loss of competitive positioning and distorted external dynamics (stemming from the subsidies) will lead to a devaluation of the Egyptian pound.

These core views lead to many derivative possibilities, notably in the value chain of goods, commodities and materials, which is why QH has also invested in businesses that should benefit from more basic dynamics, such as demographics and rising standards of living. Segments such as cement, mining and agri-food are examples of this.

Business model and strategy

The business model has evolved from private equity to investment company

Before it became QH, the company was known as Citadel Capital and operated as a private equity firm. Under the private equity model, Citadel Capital raised equity to be invested through funds, and co-invested alongside investors in the various assets that it bought. In contrast, as an investment company, Qalaa Holdings aims to be a majority owner in all its assets (and charges no management fees).

Why the switch?

We believe there are three main reasons behind the switch in business models.

- Egypt's revolution practically closed markets, making it all but impossible to monetise assets.
- Operating conditions for the private sector deteriorated owing to the economic downturn, significantly complicating access to funding.

- Citadel Capital lacked bandwidth to deal with its 19 investments, and had to refocus around a few core themes to maximise resources and returns.

Management believes that switching models will result in a simpler structure with a stronger balance sheet, and one that can more easily allocate resources (funding and management) to where they are needed in order to ultimately boost returns.

Strategy for QH as a holding company

For QH as a holding company, the medium-term plans are as follows.

- Further increase its ownership in the underlying assets.
- Exit non-core assets.
- Divest discontinued operations.
- Deleverage.
- Fund growth opportunities at existing subsidiaries.

Exiting non-core assets: This process has already begun with the sale of Sudanese-Egyptian Bank and Sphinx Glass, and QH expects more sales of non-core assets in the near and medium term. QH has given fairly detailed guidance on the expected pace and profitability of potential exits (c. 15 exits between now and 2019E for a total consideration of c. $1.2bn, of which c. $800mn will accrue to QH).

Figure 13: Guidance on possible exits and uses of proceeds, $mn

Estimated exit proceeds	1,250
Proceeds to QH	790
Of which: used to delever QH	-290
Of which: used to delever companies	-170
Of which: fund growth	-170
Of which: fund working capital for five years	-100
Of which: single acquisition	-60
	-790

Source: Company data

We are generally in favour of asset sales and deleveraging, but have limited confidence in predicting asset values or the timing of sales. For us, the value of the company guidance on asset sales is that it shows QH management to have a detailed idea about what to do with the non-core portfolio. For our valuation we take the cost value – not the expected sale value – of these investments.

We also note that many non-core assets are loss-making, inflicting losses on the consolidated QH P&L and giving another incentive to sell them. QH has reclassified many of these loss-making companies as ‘assets held for sale’.

As regards the other two parts of the holding company strategy mentioned above, namely deleveraging and funding growth, these are tied to the pace and profitability of potential exits from non-core assets.

Operational strategy for key assets

- **Cement (Asec):** The current and near-term priority will be to convert at least two plants to coal and to introduce waste-heat recovery systems. The use of refuse-

derived fuel will also contribute to improving the total energy mix. Additional capacity could also come online.

- **ERC:** Continue with construction and be ready for an expected start of operations in 1Q17.

- **Taqa Arabia:** Continue with the addition of new retail and industrial customers to gas distribution, and grow the number of fuel stations to around 100 (from 37 currently). Taqa Arabia also aims to significantly ramp up its construction and operation of power stations, by taking advantage of new coal-import laws. The company could also build power stations in the medium term.

- **Nile Logistics:** Continue to make market share gains in stevedoring and set up further strategic locations to position for coal and other large-scale imports.

- **Africa Railways:** Continue its five-year turnaround programme, focused on the rehabilitation of wagons and on acquiring new locomotives. This should help to drive volume growth and revenue per tonne-km.

Management and track record

QH's executive committee consists of the following members.

Ahmed Heikal (Chairman & Founder) completed a Masters and a PhD in Industrial Engineering and Engineering Management at Stanford University. Prior to founding Citadel Capital in 2004, he was an executive board member at EFG-Hermes, where he variously ran Asset Management, Securities, Investment Banking and Private Equity.

Hisham al Khazindar (MD and Co-founder) holds an MBA from Harvard Business School. Prior to founding Citadel Capital, he was a senior member of the Investment Banking team at EFG-Hermes.

Karim Sadek (MD, Transport & Logistics division) holds a Masters in International Securities, Investments and Banking from Reading University. Prior to joining Citadel Capital, he was an MD at a leading private equity firm in Egypt, and also worked in corporate banking and in credit at CIB and Arab Bank.

Moataz Farouk (CFO) joined Citadel Capital in 2006, prior to which he was a senior finance executive of a local subsidiary of Heineken International. Earlier in his career he also worked at Procter & Gamble and EFG-Hermes.

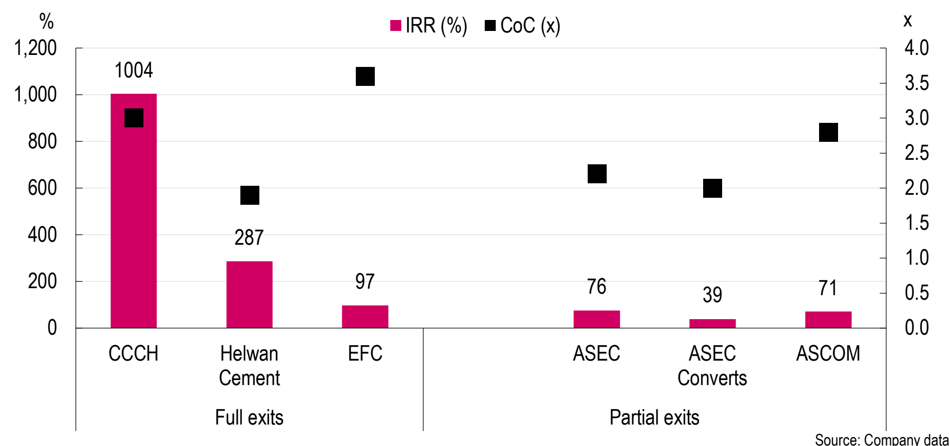
Mohamed Shoeib (MD, Energy division) is a leading industry expert in upstream and downstream energy. Prior to joining Citadel Capital, he ran the Egyptian Natural Gas Holding Company (EGAS), prior to which he was Vice-Chairman for operations at the Egyptian General Petroleum Company (EGPC).

Amr El-Garhy (MD, Agri-foods and head of corporate finance and investment review) joined Citadel Capital from the National Investment Bank, where he served as Vice-Chairman. Earlier in his career he was Deputy CFO at a Qatari bank, and MD at EFG-Hermes.

We find the firm's track record of interest, although in our view not as relevant as it was under the private equity model. Citadel Capital exited some investments in 2004, 2005 and 2007 and achieved exceptional IRRs and cash-on-cash (CoC) returns. However, with an average holding period of just 11 months for the three full exits, a sense of market

timing is likely to have been a greater factor in realising value than the more mundane task of driving through operational enhancements. What the track record shows above all else, in our view, is that management understands buying and selling assets.

Figure 14: QH – full and partial exits



Source: Company data

QH also disposed of three assets in 2013/2014, namely two subsidiaries of United Foundries Co and Sphinx Glass. We consider Sphinx Glass as an exit, since that asset was profitable and QH realised a CoC multiple of 1.25x on the transaction. As regards the metallurgy assets, we would label these as divestitures, since they were loss-making subsidiaries labelled as 'discontinued operations' in QH's financial statements. The sale of these plants is neutral to QH from a P&L perspective.

In light of the short holding periods for the early exits where high returns were achieved, and more modest ones where longer periods were required, we think the firm has yet to deliver a track record as a long-term value creator.

Corporate governance

Corporate governance is an important investment consideration to us. In the case of QH, we think the industries and geographies that the firm invests in could easily lend themselves to misperceptions.

We think the following points are relevant.

- The board of directors is evenly split between executive and non-executive directors, and members of the Audit and Compensation committees are exclusively non-executive board members. Non-executive members are appointed by shareholders.

- QH has started a programme that focuses on institutionalisation at the holding company and subsidiary levels and has appointed its first full-time Head of Audit, reporting to the Audit Committee. The position includes board-level representation at subsidiaries.

Valuation summary

We derive forecasts for ERC, Asec, Taqa Arabia, Tawazon, Nile Logistics and Africa Railways, and use relevant industry benchmarks to value them. We take the rest at investment cost, with adjustments where necessary, or at market value if available.

We summarise our valuation of QH below. The market is currently assigning zero value to many assets, in our view, as well as a holding company discount that is likely in excess of our own. We believe part of the reason may be that the valuations used in the swaps with co-investors were inferior to what we think could be construed as fair value, or that the company's profile has in recent years not been appealing to the market owing to its complexity and the inability to monetise assets via exits. The investment case – which we think is simple in aggregate – does take more work to gain comfort with than traditional mono-line businesses.

On ERC, the range of peers is 5-6x EV/EBITDA for 2016E, on Bloomberg consensus estimates, but in scenarios where that year is mostly considered to be unexceptional, as peers' operations are mature. In the case of ERC, the first full year of operations is due in 2018, so we have taken a slight liberty with this multiple in assigning it to that year.

On Asec, we have cement valued against peers on EV-based multiples, but for the construction, engineering and maintenance business we have simply taken the backlog of Aresco – the key earnings driver for those businesses – assumed a net profit margin that is in line with peers, and assigned it a multiple. We have done similarly for the cement engineering business. For Asec Holdings' stake in Misr Qena, which is 27.6%, we have divided that stake by QH's ownership in Asec to get to a proportional ownership percentage. We have also valued a single cement production line (Djelfa) at an estimated exit value below cost.

We have chosen to value assets such as Wafra and Mashreq below book value (cost), owing to limited visibility and the current lack of earnings.

Figure 15: QH – valuation summary

	Valuation method	EGPmn value	% ownership	Value to QH, EGPmn	Per share, EGP
ERC	Peers - 6x EV/EBITDA (2018E)	12,167	15.2%	1,849	1.16
Taqa Arabia	Peers - 12.1x PE (2016E)	3,483	62.5%	2,177	1.36
Tawazon	Peers - 17.2x PE (2016E)	1,185	47.9%	568	0.35
Asec Cement	Peers -6x EV/EBITDA (2016E)	1,630	69.2%	1,128	0.70
Asec Cement - direct stake	Peers -6x EV/EBITDA (2016E)	1,630	4.9%	80	0.05
Asec Cement stake in MQN	Market	2,390	19.1%	457	0.29
Asec - rest	Peers - 10x PE (2016E)	936	69.2%	648	0.40
Asec - Djelfa line sale	33% discount to cost	960	69.2%	664	0.42
Nile Logistics	Peers - 15.2x PE (2016E)	135	62.0%	84	0.05
Africa Railways	Peers - 15.2x PE (2016E)	448	30.8%	138	0.09
Gozour	QH investment cost	762	43.1%	762	0.48
Wafra	Half of QH investment cost	93	100%	93	0.06
Mashreq	Half of QH investment cost	34	54.9%	34	0.02
ASCOM	Market	380	39.2%	149	0.09
Bonyan	QH investment cost	279	60.2%	279	0.17
Tanweer	QH investment cost	166	99.8%	166	0.10
Grandview	QH investment cost	288	42.8%	288	0.18
Finance Unlimited	QH investment cost	232	99.9%	232	0.15
Glass Works	QH investment cost	140	47.6%	140	0.09
United Foundries	QH investment cost	266	67.4%	266	0.17
Total		**27,604**		**10,201**	**6.38**
Holding company debt				-2,120	-1.33
Value of QH equity				8,081	5.05
Holding company discount				10%	-0.51
Adj. value of QH equity				**7,273**	**4.55**

Source: Company data, Renaissance Capital estimates, Bloomberg

A suitable holding company discount

Investment companies and conglomerates typically trade at a discount to the aggregate value of their parts, as value realisation inevitably gets diluted by shareholder or capital structures and diversity of businesses and geographies and so on.

With this company, we think the market is also going to apply a holding company discount, but we note that the thematic anchor of most of the companies in Qalaa Holding's portfolio is energy, either directly or indirectly. Moreover, we see an argument for recognising the holding company's management capacity to cross-pollinate its businesses, such that separate companies can and often do work together. In fact, certain companies such as Asec and Ascom have businesses that are complementary (cement and quarries), and we think future intra-portfolio synergies will be important to look out for, such as between Nile Logistics and Asec and/or Taqa Arabia, and between Taqa Arabia and others. Our point is that in the case of this holding company, driving synergies should be a natural development, given the complementary sectors in which its companies operate. Recognising this, we have opted for a 10% discount to aggregate value. However, we believe the market could accept a discount of up to 20%.

Risks

Key risks to our forecasts include a changing regulatory landscape, in downstream energy and other segments, as energy policy evolves. ERC and Taqa Arabia could be exposed to such risks, as could Asec Holding and Tawazon, to a lesser degree.

Some execution risk is also latent in greenfield projects. Macro volatility could also result in additional pricing risk on key commodities.

The market is expecting one more swap transaction for QH to complete its transformation

Mechanics and practicalities of the switch from private equity to investment company

To effect the switch away from private equity into an investment company, QH is buying out its former co-investors in the funds that it managed on their behalf. In lieu of cash, QH is issuing new shares with which to pay, and swapping these against increased economic ownership in the underlying assets.

The valuations that formed the basis of the first swap transaction (April 2013) were based on work done by a third-party independent valuation firm (Riscura), and aimed to reflect end-2011 values. The effective date of 31 December 2011 was chosen because agreements with co-investors were reach in 1H12.

Based on these valuations, QH and co-investors determined an exchange ratio between percentage of ownership in the underlying assets and the number of QH shares (at par value, or a 16% discount to the value of QH shares, according to Riscura). As per the valuations realised in the swap transactions, **QH and its co-investors valued the equity of the underlying assets at $1.5bn**.

Figure 16: 2013 swap transaction valuations

	Ownership, %			Riscura stake val pre swap, EPGmn	Implied val for 100% stake, EPGmn	Base val for swaps (84%), EPGmn	Swap amounts, EPGmn	Current value of QH stake, EPGmn	Implied val 100%, EPGmn	Riscura stake val pre swap, $mn	Implied val for 100% stake, $mn	Base val for swaps (84%), $mn	Swap amounts, $mn	Current value of QH stake, $mn	Implied val 100%, $mn
	Pre	Post	Diff												
Taqa Arabia	33.8%	62.5%	28.7%	655	1,938	1,628	467	1,123	1,796	82	242	204	58	140	225
Tawazon	47.9%	47.9%	0.0%	58	121	101	0	58	121	7	15	13	0	7	15
ERC	11.7%	15.2%	3.5%	341	2,915	2,449	86	427	2,808	43	364	306	11	53	351
Mashreq	24.5%	54.9%	30.4%	39	161	135	41	80	147	5	20	17	5	10	18
Nile Logistics	37.9%	62.0%	24.1%	187	492	413	100	286	461	23	62	52	12	36	58
Africa Railways	28.2%	30.8%	2.6%	251	888	746	19	270	876	31	111	93	2	34	110
Gozour	20.0%	43.1%	23.1%	297	1,484	1,247	288	585	1,357	37	186	156	36	73	170
Wafra	100.0%	100.0%	0.0%	186	186	156	0	186	186	23	23	20	0	23	23
ASCOM	39.2%	39.2%	0.0%	104	265	223	0	104	265	13	33	28	0	13	33
Asec Holding	54.8%	69.2%	14.4%	930	1,698	1,426	205	1,136	1,641	116	212	178	26	142	205
GlassWorks	21.0%	47.6%	26.6%	160	764	642	171	331	696	20	95	80	21	41	87
United Foundries	30.0%	67.4%	37.4%	144	480	403	151	295	438	18	60	50	19	37	55
Finance unlimited	99.9%	99.9%	0.0%	230	230	194	0	230	230	29	29	24	0	29	29
Bonyan	32.1%	60.2%	28.1%	154	480	403	113	267	444	19	60	50	14	33	56
Grandview	13.0%	42.8%	29.8%	119	914	768	229	348	812	15	114	96	29	43	102
				3,856	**13,018**	**10,935**	**1,870**	**5,726**	**12,278**	**539**	**1,821**	**1,529**	**262**	**801**	**1,535**

Source: Company data, Renaissance Capital estimates

Citadel Capital issued 728.375mn new shares in April 2013 at a par value of EGP5, resulting in a capital increase of EGP3.642bn (c. 84% dilution). From this amount, EGP1.87bn was used to cover the swap transactions with co-investors (c. 374mn shares at par), EGP910mn was purchased by CCP, and most of the balance was used to buy back debt on an asset that was written down to zero in 2013 (we do not know the valuations on that transaction).

Figure 17: Capital raise proceeds and uses, EGP

	Pre swap	Post swap
No. of shares	871,625,000	1,600,000,000
Of which common	653,718,750	1,200,000,000
Of which preferred	217,906,250	400,000,000
New shares issued		728,375,000
Par value		5
Value of new capital issued		3,641,875,000
Amount paid to increase stake in companies		**1,870,078,150**
Balance		1,771,796,850
Amount subscribed by CCP		910,468,750
Amount used to buy back debt		650,000,000
Balance		211,328,100

Source: Company data

QH management has guided for another swap transaction in 2015.

Senior management, via the CCP vehicle, own some 26% of the outstanding QH stock, and so has a lot at stake personally in the success of the firm. This provides some level of comfort as to the alignment of management with minority shareholders, in our view. CCP will maintain its ownership level at current levels, meaning that senior management will have to put a lot more money into the company.

Further issuance of stock at par value should lift the market price, if only temporarily. Should QH issue a further 500mn shares, for example, the fact that issuance takes place at par value (EGP5), which is higher than the current market price, means that the overall price will be raised.

In light of the above, and since our own SoTP valuation is higher than market value, we believe the swap transactions should be welcomed by minority shareholders. The only caveat is that the investors swapping their shares in the underlying companies for shares in the holding company are bound by a one-year lock up agreement. If such investors accepted the discount to fair value in exchange for a near-term exit strategy, assuming that they may be sellers of the stock at the earliest given opportunity is only logical. Consequently, we believe the stock is likely to show periods of volatility on the expiry of such lock-up agreements, and if more swaps are forthcoming, more volatility could follow.

Overview of key assets

Asec Holding (cement)

Asec Holding (legally known as National Development and Trading Company [NDT]) is currently the largest company in the QH portfolio. It was created in 1975 as a JV between Holcim Cement and local cement companies as the Arab Swiss Engineering Company (ASEC). Citadel capital acquired a stake in 2004 and restructured the business to focus on three core businesses: 1) cement production; 2) engineering, management and consulting; and 3) construction and contracting. Foundries and mining were spun off into United Foundries and Ascom, both of which remain to this day in QH portfolio (foundries non-core). Through its subsidiaries, Asec Holding has a presence in the Middle East and Africa, including Egypt, Sudan, Algeria, Jordan, and Mozambique.

Today, Asec Holding's portfolio includes

1. Cement production through Asec Cement and its subsidiaries.
2. Engineering, management and consulting through its subsidiaries Asec Engineering and Asenpro.
3. Construction and contracting through its subsidiaries Aresco and Asec Automation.

Asec Cement

Asec Cement's capacities can be broken down as follows: owned capacity (Asec Minya and Takamol) 3.6mn tpa; influenced capacity (Misr Qena) 2.0mn tpa; and held-for-sale capacity (Zahana) 1.0mn tpa, in addition to Asec Cement's Djelfa greenfield project in Algeria, of 3.4mn pta, which is also currently being divested.

Asec Cement also owns 55% of a ready-mix business, Asec Ready Mix, with Misr Qena owning the remaining 45%. Asec Ready Mix is a market leader in Upper Egypt, with production volume of 335,000 m3 in 2014E, according to company data.

Figure 18: Asec Cement production facilities and capacity

Country	Name	Capacity in mtpa	Ownership status	%
Egypt	Asec Minya	2.0	Subsidiary	50.0%
Egypt	Mirs Qena	2.0	Associate	27.6%
North Sudan	Al-Takamol Cement	1.6	Subsidiary	51.0%
Algeria	Zahana Cement	1.0	Held for sale	35%
Algeria	Asec Algeria Cement (Djelfa) - Greenfield	3.4	Held for sale	72.3%
Total		10.0		
Asec Cement influenced		5.6		
Asec Cement owned		3.6		

Source: Company data

We expect the current ownership and production capacity structure to change in the near term, as QH intends to sell the Algerian assets and increase its domestic production in Egypt.

Domestic dynamics are supportive, and a switch to coal and other cost enhancements should support rising margins

We see the near-term drivers of cement consumption in Egypt as increased government spending on key infrastructure projects and rising private-sector spending. Data from the Central Bank of Egypt suggest that cement consumption was c. 46.6mnt in 2014, with anaemic growth rates in recent years reflecting subdued economic conditions. We therefore believe a spending-led rebound should be the main driver of volume growth in the near term.

Beyond the issue of volume, a major operational shift is taking place as a result of the government's decisions to gradually energy cut subsidies. The acute shortage of energy supplies in recent years – and particularly in 2014 – has disrupted feedstock supplies to cement producers and materially increased production costs. Capacity utilisation levels have also suffered. Faced with rising feedstock costs, cement products are now focused on diversifying their energy mix and driving through efficiency initiatives. The government's recent decision to allow private sector coal imports is already leading many cement producers to make the switch to coal, and other alternatives such as biomass and refuse-derived fuels are also increasing their share (albeit from a low base). We therefore see the second major driver for the cement industry in Egypt in the near term as changing energy sources and the drive for greater efficiency.

We have assumed both rising volumes and improving efficiency in our earnings assumptions for the cement business.

Asec's controlled capacity is currently in Upper Egypt and North Sudan

The main plant is Asec Minya, located in the south of Egypt. This greenfield project launched in 2013 amid political turmoil and a great deal of uncertainty, but nevertheless has managed a strong start, in our view. The local market in the south is more fragmented than in larger metropolitan areas in the north, and is under-served by the established large players, creating what we see as a good niche opportunity to capture demand without having to sacrifice pricing. Current capacity stands at 2.0mn tpa, but a brownfield expansion could bring this up by a further 2.0mn tpa by around 2017, on our estimates. Other key developments include connecting to the national grid in the near term, driving efficiencies with the use of a waste heat-recovery project, and the use of biomass and refuse-derived fuel. A switch to coal/pet coke is also under way.

Asec's second asset, Al Takamol, is located in North Sudan. This is a 1.6mn tpa plant that caters to an under-served market, where pricing is highly dependent on the government's imports of fuel. Although the plant is guaranteed electricity by an on-site, fully-owned power plant, fuel and power prices are volatile. However, demand has proved solid and we expect margins to rise with the introduction of pet coke and coal as burnable fuel sources.

Our forecasts and assumptions

On an aggregate basis, we forecast actual production to roughly double by 2018, to 4.5mnt, from 2.1mnt in 2014E. We expect the normalised EBITDA margin to rise to c. 32.4%, from 28.5% in FY14E. We think the cement business could generate some EGP827mn in EBITDA by 2016E.

Figure 19: Asec Cement assumptions and forecasts

	FY14E	FY15E	FY16E	FY17E	FY18E
Asec Menya					
Cement capacity, mnt	2.0	2.0	2.0	4.0	4.0
Utilisation %	80%	90%	95%	70%	80%
Cement volume, mnt	1.6	1.8	1.9	2.8	3.2
YoY growth		12.5%	5.6%	47.4%	14.3%
Revenue/tonne, EGP	797.5	877.3	894.8	912.7	940.1
YoY growth		10.0%	2.0%	2.0%	3.0%
Revenue, EGPmn	1,276.0	1,579.1	1,700.1	2,555.5	3,008.2
YoY Growth		23.8%	7.7%	50.3%	17.7%
EBITDA/tonne, EGP	255.2	307.0	326.6	337.7	357.2
YoY growth		20.3%	6.4%	3.4%	5.8%
EBITDA, EGPmn	408.3	552.7	620.5	945.5	1,143.1
YoY growth		35.4%	12.3%	52.4%	20.9%
EBITDA margin	32.0%	35.0%	36.5%	37.0%	38.0%
Al Takamol					
Cement capacity, mnt	1.6	1.6	1.6	1.6	1.6
Utilisation	33%	60%	65%	70%	80%
Cement volume, mnt	0.5	1.0	1.0	1.1	1.3
YoY growth	-23%	82%	8%	8%	14%
Revenue/tonne, SDG	517.5	569.3	597.7	621.6	640.3
YoY growth	0.2	0.1	0.1	0.0	0.0
Revenue, SDGmn	273.2	546.5	621.6	696.2	819.5
YoY growth	-11.7%	100.0%	13.8%	12.0%	17.7%
EBITDA, SDGmn	41.0	91.8	120.6	137.9	164.7
EBITDA margin	15.0%	16.8%	19.4%	19.8%	20.1%
EGP/SDG exchange rate	1.3	1.8	1.8	1.8	1.8
Revenue, EGPmn	341.6	983.7	1,118.9	1,253.2	1,475.2
YoY growth	-2.4%	188.0%	13.8%	12.0%	17.7%
EBITDA, EGPmn	51.2	165.3	217.1	248.1	296.5
YoY Growth (%)	192.9%	222.6%	31.4%	14.3%	19.5%
Combined					
Capacity, mnt	3.6	3.6	3.6	5.6	5.6
Utilisation	59%	77%	82%	70%	80%
Volume, mnt	2.1	2.8	2.9	3.9	4.5
Revenue, EGPmn	1,617.6	2,562.7	2,819.0	3,808.7	4,483.4
EBITDA, EGPmn	**459.6**	**717.9**	**837.6**	**1,193.7**	**1,439.6**
EBITDA margin	28.4%	28.0%	29.7%	31.3%	32.1%
EBITDA/tonne, EGP	127.7	199.4	232.7	213.2	257.1
EBITDA/tonne, $	16.0	24.9	29.1	26.6	32.1

Source: Company data, Renaissance Capital estimates

In terms of valuation, the EV/tonne of a wide sample of emerging market (EM) peers at $83 would suggest an EV of EGP2.4bn,although we think this is fairly punishing for Asec given the future capacity ramp-up we expect. Moreover, this EV would represent only 3.4x our forecast 2015E EBITDA, likely a large discount to most local and international peers. We think a multiple of 6x 2015E is fair, where international EM peers trade at 9.5x 2014 and 11x 2013. This would give us an implied EV of EGP4.3bn, or an equity value of EGP3.2bn (adjusting for expected net debt of 1.1bn). Asec Holding owns 51% of the cement capacities, so we would adjust this number again (*0.51), and once more to account for QH's ownership in Asec Holding. The attributable equity value to QH would be EGP1,145, or 0.72 per QH share. To this we add QH's direct stake in Asec Cement, 4.9% (EGP1,635mn, which is the equity value attributable to Asec Holding, * 4.9%). This brings the total value of the cement business, to QH, to EGP1,225mn, or EGP0.77/share.

Figure 20: Cement peer group

	Country	Capacity, mn tpa	Last price, LC	MktCap, $mn	EV/EBITDA, x 2013	EBITDA margin, % last published	EBITDA/ tonne, $	EV/tonne, $
SSA cement companies								
ARM Cement Ltd	Kenya	3.05	81.5	441	16.05	20.79	11.23	180.17
Bamburi Cement Co Ltd	Kenya	3.55	154	611	6.70	21.77	23.88	159.93
Ashaka Cem plc	Nigeria	1.2	20.29	236	12.59	29.62	22.02	277.10
Cement Co Northern Nigeria plc	Nigeria	0.5	9.07	59	5.78	8.00	34.01	196.50
Tanzania Portland Cement Company	Tanzania	1.3	4000	395	12.26	28.00	29.62	363.01
Tanga Cement Company	Tanzania	1.25	4830	169	5.91	28.00	25.76	152.15
Turkey cement companies								
Adana Cimento Sanayii TAS	Turkey	7.8	6.5	443	7.83	28.85	4.92	38.56
Afyon Cimento Sanayi TAS	Turkey	1.2	120	153	-25.32	17.93	-2.11	53.51
Akcansa Cimento AS	Turkey	15.9	18.1	1,469	11.04	27.78	7.53	83.19
Bolu Cimento Sanayii AS	Turkey	5.5	6.05	367	12.29	31.24	3.85	47.26
BatiSoke Soke Cimento Sanayii TAS	Turkey	2.4	2.87	96	28.26	29.21	1.35	38.23
Baticim Bati Anadolu Cimento Sanayii AS	Turkey	3.2	7.54	256	18.67	22.28	5.39	100.65
Bursa Cimento Fabrikasi AS	Turkey	4.3	5.74	257	32.80	15.90	2.14	70.16
Cimsa Cimento Sanayi VE Ticaret AS	Turkey	11.9	17.25	988	8.54	26.45	9.82	83.84
Cimentas AS	Turkey	9.5	9.2	340	10.47	20.16	4.04	42.26
Goltas Goller Bolgesi Cimento Sanayi ve Ticaret AS	Turkey	4.8	78.1	238	7.59	25.78	6.47	49.06
Konya Cimento Sanayii AS	Turkey	3.5	332.5	687	17.12	22.95	7.71	131.96
Mardin Cimento Sanayii ve Ticaret AS	Turkey	5.0	5.16	240	7.51	34.73	5.77	43.29
Nuh Cimento Sanayi AS	Turkey	10.1	11.1	707	11.51	26.86	6.37	73.34
Unye Cimento Sanayii Ve Ticaret AS	Turkey	4.1	5.38	282	5.08	32.64	11.09	56.33
UAE cement companies								
Arkan Building Materials	UAE	5.5	1.1	519.3	95.96	16.14	2.01	193.15
Gulf Cement Company	UAE	3	1.1	241.4	164.15	14.38	0.55	89.60
Fujairah Cement Industries	UAE	4	1.4	130.8	11.10	9.73	6.75	74.98
Sharjah Cement and Industrial Company	UAE	4.25	1.2	173.1	12.15	11.71	4.73	57.46
Union Cement Company	UAE	4.5	1.3	236.9	9.23	24.87	5.66	52.21
Pakistan cement companies								
Cherat Cement company	Pakistan	1.1	80	139	4.62	29.52	16.34	75.41
Lafarge Pakistan	Pakistan	2	18	255	9.21	21.84	15.12	139.30
Lucky Cement	Pakistan	7.5	549	1,757	10.37	24.39	17.11	177.39
Malaysia cement companies								
Tasek Corporation Berhad	Malaysia	2.3	15	512	11.02	24.30	19.02	209.57
Cahya Mata Sarawak Berhad	Malaysia	2.5	4	1,206	14.18	25.84	33.44	474.11
Median					**11.03**	**24.63**	**7.14**	**83.51**

Note: Prices as at 27 January 2015.

Source: Bloomberg

The other parts of Asec – engineering, construction and contracting

We have to rely more on company guidance for this side of the business, and the company has shared Aresco's backlog information with us. The backlog stands at EGP1.7bn, and guidance is for an EBITDA margin of 8% on revenue of c. EGP850mn in 2015E, suggesting EBITDA of EGP68mn.

In engineering, we expect revenue to be c. EGP650mn on an EBITDA margin of 13% (EBITDA of EGP84.5mn). Looking at peer data, we find that companies tend to operate with a median net profit margin of 4.4%. If we apply the same margin to Aresco and Asec Engineering, this would imply net income of EGP66mn. Applying the forward peer multiple of 14.2x would value these two businesses at EGP936mn, of which 69.2% would be attributable to QH. On a per-share basis, this equates to EGP0.4.

Figure 21: Cement EPC peers

Ticker	Name	MktCap, $mn	Last price, $	EBITDA margin, %	Net profit margin, %	P/E FY1, x
FLS DC Equity	Flsmidth & CO A/S	2,172	42.4	7.5	1.6	19.93
MEO1V FH Equity	Metso OYJ	4,522	30.1	12.5	7.2	14.19
OTE1V FH Equity	Outotec OYJ	1,082	5.9	4.6	0.9	16.37
ASTE US Equity	Astec Industries Inc	831	36.3	7.7	3.6	
MTU FP Equity	Manitou BF	583	14.7	5.9	1.1	19.20
WAC GR Equity	Wacker Neuson SE	1,388	19.8	15.8	7.2	13.92
FENR LN Equity	Fenner plc	603	3.1	14.0	3.1	10.78
JOY US Equity	Joy Global Inc	4,020	41.3	17.2	8.8	13.33
TEX US Equity	Terex Corp	2,435	22.5	8.7	4.4	9.92
600031 CH Equity	Sany Heavy Industry Co Ltd-A	10,437	1.4		4.5	
PIG FP Equity	Haulotte Group	454	14.5	9.2	2.0	19.20
ATCOA SS Equity	Atlas Copco AB-A	35,102	29.3	22.2	13.1	
PON1V FH Equity	Ponsse OYJ	391	14.0	12.1	7.2	11.27
SAND SS Equity	Sandvik AB	11,894	9.5	14.4	5.2	16.65
000680 CH Equity	Shantui Construction Machi-A	1,464	1.2		2.1	

Note: Prices as at 27 January 2015.

Source: Bloomberg

Egyptian Refinery Company (ERC)

ERC is a $3.7bn second-stage refinery project that will operate as a hydro-cracking facility, taking in fuel oil produced by an existing facility (Cairo Oil Refinery Company [CORC]) and processing this feedstock into more complex refined products. The combined Nelson complexity of both facilities is c. 8 (implying a lower complexity for CORC and a higher one for ERC).

ERC's intake of feedstock is based on state guarantees (via CORC) for the provision of at least 3.5mn tpa of fuel oil, priced at premium of 4.4% to market to account for the variance in viscosity. ERC will purchase a further 1.2mn tpa of Arabia medium crude, which it will pay CORC a fixed $3/bl to process, bringing its total intake to 4.7mn tpa.

With this feedstock, ERC will produce a variety of higher-grade products, including diesel and jet, and sell c. 88% of its output to the Egyptian Gas and Petroleum Co (EGPC), based on off-take agreements at international prices. The remaining lower-margin products will be sold on the open market.

Figure 22: Feedstock and output of ERC, kt

Product	Input	% total	Product	Output	% total	Sold to
Crude	1,200	26%	Fuel oil	315	7%	EGPC
Fuel oil	3,500	74%	Naphta	336	7%	EGPC
			Reformate	522	11%	EGPC
			Jet	599	13%	EGPC
			Diesel	2,255	48%	EGPC
			LPG	79	2%	EGPC
			Coke	453	10%	Market
			Sulfur	96	2%	Market
Total	**4,700**	**100%**		**4,655**	**100%**	

Source: Company data

The cost of the project is $3.7bn, including $2.35bn in debt. Financing was agreed in 2Q12 and management expects the facility to start operating in 1Q17; around 35% of the construction is complete.

Figure 23: Sources and uses of funds, ERC

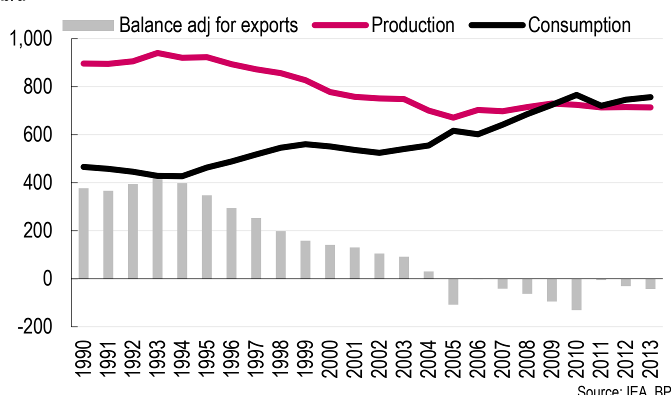
Uses of funds	$mn	%	Sources of funds	$mn	%
Capex			**Debt**		
EPC contract	*2,195*	*59.20%*	*KEXIM loan facility*	*620*	*16.70%*
Owner's costs	*800*	*21.60%*	*KEXIM-guaranteed facility*	*180*	*4.90%*
Contingency	*85*	*2.30%*	*JBIC loan facility*	*540*	*14.60%*
Total capex	**3,080**	**83.10%**	*NEXI covered facility*	*360*	*9.70%*
			AfDB facility	*200*	*5.40%*
IDC, fees, premium & financing contingency			*EIB loan facility*	*450*	*12.10%*
Financing contingency	*2*	*0.00%*	**Total debt**	**2,350**	**63.40%**
IDC, fees & premium	*611*	*16.50%*			
Swaption and waiver fee	*6*	*0.20%*	**Equity**		
Total IDC, fees, premium & financing contingency	**618**	**16.70%**	*Base equity*	*1,134*	*30.60%*
			Contractor subordinated loan	*200*	*5.40%*
Prepayment of the processing fee	10	0.30%	*AfDB subordinated convertible mezzanine*	*25*	*0.70%*
			Total equity	*1,359*	*36.60%*
Total uses	**3,709**	**100%**	*Additional equity/(refund of equity)*	*0*	*0.00%*
			Total equity	**1,359**	**36.60%**
			Total sources	**3,709**	**100%**

Source: Company data

Domestic energy situation makes ERC a project of national significance

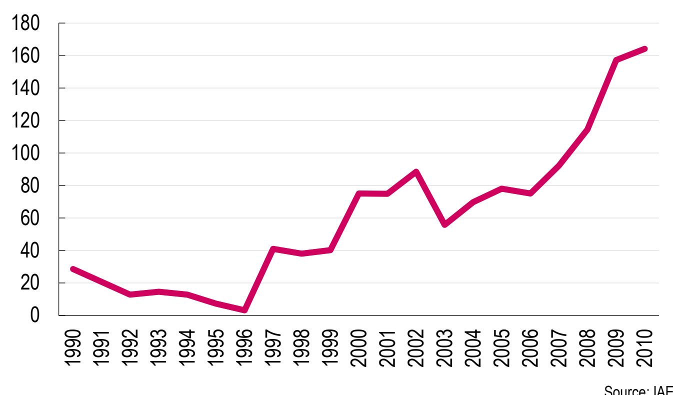
Egypt became a net energy importer in the mid-2000s, owing to a lack of investment in domestic production, rising consumption and uneconomic subsidies.

Figure 24: Egypt – oil production, consumption, and export-adjusted balance, kb/d



Source: IEA, BP

Figure 25: Egypt – imports of refined products, kb/d



Source: IAE

Existing refining capacity stands at some 760kb/d, around 160kb/d below demand at 2010 levels, implying that demand is close to 1mmb/d, assuming some demand growth owing to the country's economic recovery.

Figure 26: Egypt refinery capacity, b/d

Refinery	Start-up	Location	Capacity
AMOC	2002	Alexandria	34,447
MIDOR	2001	Alexandria	100,000
Assiut	1987	Assiut	47,000
Tanta	1973	Tanta	35,000
Ameriya	1972	Alexandria	78,000
Cairo	1969	Cairo	160,000
Alexandria	1957	Alexandria	100,000
El-Suez	1921	Suez	66,400
El-Nasr	1913	Suez	146,300
Total			**767,147**

Source: Company data

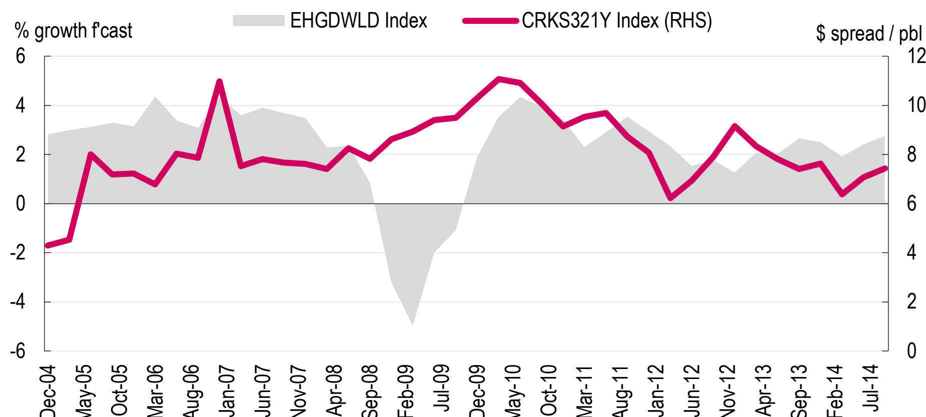
ERC's projected output is c. 90kb/d

ERC's product specificity is targeted precisely at the grade levels that we expect to see growing shortages, namely middle distillates such as diesel, jet fuel and gasoline (diesel alone accounts for c. 40% of Egypt's refined imports). In contrast, heavy fuels such as fuel oil should see lower demand, supporting the economic rational for using those as feedstock to produce more complex products. Since EGPC is buying 80% of the output, ERC is sheltered from some volatility.

In the end, the price of crude and its derivatives is what matters

We think ERC is assured strong backing by all its stakeholders (EGPC owns c. 24% of the project). However, the key to its margins is oil prices and the spread between input and output, rather than Egypt's specific energy situation. This is because roughly 75% of the feedstock and 88% of the output are procured and sold to the same entity based on international market prices, so there is little flexibility on volume, such that price is the main determinant of spreads. We think correlations with global price cycles are likely. Historical crack spread data suggest a variance of around $6/bl.

Figure 27: World GDP growth vs Brent 321 crack spreads



Source: Bloomberg

Our forecast assumptions

We take a starting point of oil at $70/bl, implying fuel oil at c. $388/t and diesel at $668/t. We assume crude going to $75/bl and then to $80/bl at steady state within two years of the start of operations. Our forecasts are currently below management guidance, likely owing to differing views on oil prices.

Figure 28: ERC summary forecasts, $mn (unless otherwise stated)

	2017E	2018E	2019E	2020E	2021E
Days of operation	250	350	350	350	350
Input volume, mnt	3.36	4.70	4.70	4.70	4.70
Input cost	1,460	2,197	2,353	2,353	2,353
Output volume, mnt	3.33	4.66	4.66	4.66	4.66
Output revenue	1,946	2,888	3,056	3,056	3,056
Gross profit	486	691	703	703	703
Gross refining margin, $/bl	20	20	21	21	21
EBITDA	418	590	602	605	608
Depreciation	-59	-46	-110	-142	-143
EBIT	358	544	493	463	466
Interest expense	0	-100	-81	-69	-57
EBT	358	445	412	394	408
Income tax	-86	-110	-104	-98	-102
Net income	272	334	308	295	306

Source: Renaissance Capital estimates

Valuation

We value ERC on the basis of EV/EBITDA multiples. Peers trade on a 2016E EV/EBITDA multiple of 5.6x, on Bloomberg consensus estimates, but with a median margin of $13.2/bl and an EBITDA margin of 3.8%. In contrast, we forecast that ERC will have a margin of c. $20/bl and an EBITDA margin of 20%. This should command a premium vs peers, in our view. We therefore apply a multiple of 6.0x to our 2018E EBITDA to reach an implied EV of $3,540mn, which we adjust for debt and cash to reach an implied equity value of $1,689mn. We use 2018E because 2017E would not represent a full year of earnings.

To account for the fact that the project is not completed yet, and that our numbers are therefore theoretical, we apply a 10% discount to the equity value, reaching $1,520 (or EGP12,167mn, assuming an exchange rate of EGP8.0/$).

Figure 29: Refining peers valuation data

Ticker	Name	Price, LC*	MktCap, $mn	EBITDA margin, %	Margin , $/bl	EV/barrel, $, x	EV/EBITDA 2016E, x	P/E 2016E, x
VLO US Equity	Valero Energy Corp	50.16	26,146	4.12	9.7	18.1	4.8	9.7
MPC US Equity	Marathon Petroleum Corp	87.16	24,422	4.85	13.2	9.4	5.9	11.5
TSO US Equity	Tesoro Corp	79.62	10,052	3.31	11.2	7.5	5.6	12.5
WNR US Equity	Western Refining Inc	35.69	3,520	6.84	18.9	6.9	5.6	10.5
DK US Equity	Delek US Holdings Inc	30.81	1,866	3.76	14.0		5.6	15.0
CLNE US Equity	Clean Energy Fuels Corp	4.4	396	na	na	12.5	na	na
PSX US Equity	Phillips 66	68.52	37,927	2.25	10.1		6.3	10.8
PTOFS TI Equity	Omv Petrol Ofisi AS - A share	5.11	1,249	2.74	na	3.2	na	na
DLEKG IT Equity	Delek Group Ltd	97030	2,846	9.70	na		na	16.1
ALJ US Equity	Alon USA Energy Inc	12.29	855	3.90	20.8		4.0	23.8
SLN1 SK Equity	Slovnaft AS	26.11	605	3.33	na		na	na
UNIP CP Equity	Unipetrol AS	138.15	1,014	1.68	na		na	na
PZOL IT Equity	Paz Oil Co Ltd	50150	1,273	3.27	na		na	na
QFLS QD Equity	Qatar Fuel Co	211.9	4,914	11.15	na		na	na
CAPL US Equity	Crossamerica Partners LP	37.78	868	2.56	na		11.9	30.5
1434 TT Equity	Formosa Taffeta Co	32.5	1,748	12.56	na		8.7	14.2
Median				**3.76**	**13.24**	**8.47**	**5.62**	**13.35**

*Priced as of 27 January 2015.

Source: Bloomberg

Risks

Downstream projects globally are subject to significant regulatory risk, and this instance is no different. Construction delays could also occur, pushing back the start date of the project.

Taqa Arabia

Taqa Arabia is a leading Egyptian independent energy distribution group. This is a roll-up investment initially acquired by Citadel Capital in 2006, reflecting the view that power generation and distribution would be critical to Egypt's future, given its precarious net energy position.

Taqa Arabia operates in three segments.

- **Downstream gas distribution,** where since 2006 it has grown to become the largest private-sector distributor of natural gas in Egypt, with long-term concessions in 11 governorates. It also has the largest downstream natural gas engineering and construction business in Egypt, handling work for the group as well as private- and public-sector clients in Egypt and the wider MENA region.

- **Power generation and distribution,** where it is was the first to acquire a license to generate and distribute electricity to third parties and is Egypt's largest power provider.

- **Oil products marketing,** where the company has a head start being the first Egyptian company to sell refined products to retail and wholesale clients. In this segment, TA also operates a network of fuelling stations that specialise in compressed natural gas.

Of the three main units, power is the main contributor to gross profits, at 45% in FY13, followed by gas (33%).

Power generation and distribution

Power generation is a critical factor for Egypt's medium- to long-term development, in our view. From a political perspective, a lack of reliable power could lead to unrest – as seen in the past – and complicate the current political transition. From an economic perspective, industrial capacity is held back by the lack of reliable power, affecting pricing dynamics, investment decisions and, ultimately, economic output. The current situation has been complicated by Egypt's subsidy policies (which are now being gradually unwound) and by bureaucracy. We believe Egypt must reform the sector and significantly grow its generation capacity, for which it will require private-sector investment.

State data indicate that installed capacity as of June 2012 was barely above peak load (assuming a c. 10% loss the reserve would be only c. 460 MW), and at that time there were existing plans to grow output significantly. We believe current tenders are in the order of 30 GW.

Figure 30: Installed and newly planned capacity in MW as at June 2012

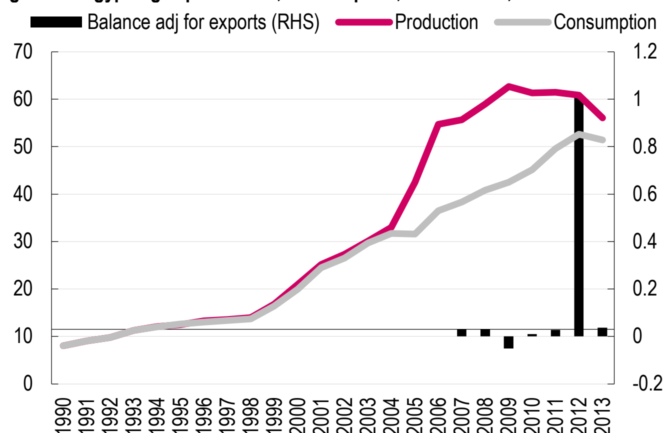
	Installed capacity	Plans for new capacity	
		Date	MW
Hydro	2,800	2012/2013	2,550
Thermal	23,539	2013/2014	3,410
Renewable	687	2014/2015	2,380
Private sector (BOOTs)/thermal	2,048	2015/2016	5,760
	29,074		**14,100**
Peak load	25,705		

Source: Egypt Electricity Holding Co

Downstream gas dynamics remain largely constrained by upstream capacity issues. Egypt's energy production has declined due to lack of investments, while domestic consumption is precariously balanced owing to export commitments, with a net balance of close to zero in recent years. The ratio of natural gas to the total fuel ratio among all

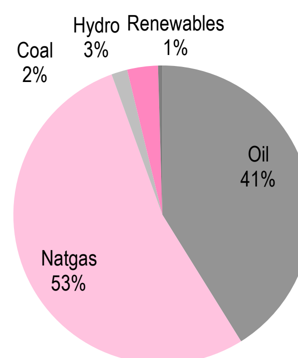
power generation companies stood at 84.3% as at June 2012, according to the National Electricity Company.

Figure 31: Egypt – gas production, consumption, and balance, bn m3



Source: BP, IEA

Figure 32: Egypt – energy use in mn toe equivalent (2013E)



Source: BP

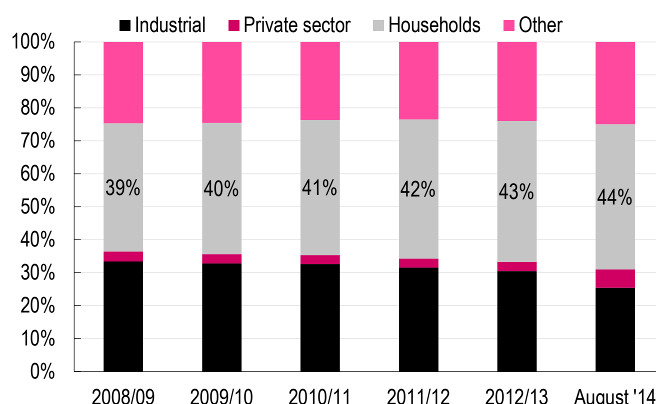
The government owns almost all (90%) of the generation and the entire distribution and transmission network. The major issue for the sector remains the stability of gas supply.

Egypt plans to import LNG and has issued tenders for several FSRUs, which could ease supply constraints in the medium term. The downstream segment has to be understood in the wider context of the upstream segment.

Figure 33: Generated power (public sector) as % of total power

Source: Central Bank of Egypt

Figure 34: Uses of generated and purchased power by segments



Source: Central Bank of Egypt

The sector's prospects shape Taqa Arabia's near-term outlook and priorities

Given sector dynamics in generation and distribution, Taqa Arabia's businesses should benefit from strong growth drivers. In the near term, its focus in terms of generation will be the construction of two gas-fired plants with a capacity of 250 MW each, in addition to the completion of smaller-scale projects currently under way. We think Taqa Arabia could also be exploring opportunities in solar power.

In distribution, the focus will be on growing penetration of the industrial and residential segments. From a base of c. 600,000 currently, TA has signed a contract with the government to connect an additional 300,000 households over the coming three years. Once homes are connected to the grid, TA can make money by collecting the float on behalf

of the National Gas Company, and by charging fees. Essentially this is a play on volumes and on fees for a fixed service. In the industrial segment, prices tend to be usage-based, and we expect further regulatory changes to allow for greater-private sector profitability.

Oil marketing division also to see strong growth

Taqa Arabia's third focus area concerns its oil marketing division. The company aims to increase the number of service stations to >100 from the current 37 by around 2018/2019. We think this could increase its sales volumes by a factor of 2x. Taqa Arabia owns a storage terminal in the Suez area, and is planning to construct a second one in Alexandria in the coming years. We note that Taqa Arabia operates its assumptions on individual, station-specific IRR targets, rather than in aggregate terms. We understand from management that each station has a minimum threshold IRR target of 18-20%, suggesting that volumes sold are a function of other factors, such as location and size.

What we assume in our numbers

The key revenue drivers, we believe, are likely to be power and oil marketing, since gas revenue is purely a function of volumes, where we expect steady but incremental gains. On the power side, we expect generation (in kWh) to increase in 2016, as some extra capacity comes on stream. We have assumed a one-time increase in prices, but concede that a gradual increase is just as likely. On the oil marketing side, we expect the increase in the number of stations to generate higher sales, but the impact of this revenue on EBITDA is limited, given the lower margins in that businesses.

Figure 35: Taqa Arabia – income statement, EGPmn (unless otherwise stated)

	2013E	2014E	2015E	2016E	2017E	2018E
Gas	393	487	578	619	688	759
Power	269	291	314	519	694	928
Oil marketing	540	807	1,321	2,180	3,429	4,862
Total revenue	**1,202**	**1,584**	**2,214**	**3,317**	**4,811**	**6,549**
YoY growth	5%	32%	40%	50%	45%	36%
Gas	-261	-360	-410	-371	-427	-471
Power	-167	-192	-182	-156	-194	-278
Oil marketing	-524	-783	-1,321	-2,093	-3,326	-4,765
Cost of sales	**-952**	**-1,335**	**-1,914**	**-2,619**	**-3,947**	**-5,514**
Revenue	79%	84%	86%	79%	82%	84%
Gross profit	249	250	300	698	864	1,035
Margin	21%	16%	14%	21%	18%	16%
YoY growth	4%	0%	20%	133%	24%	20%
Total admin expenses	-87	-94	-56	-333	-287	-249
EBITDA	**162**	**155**	**243**	**365**	**577**	**786**
Margin	13.5%	9.8%	11.0%	11.0%	12.0%	12.0%
YoY growth	12%	-4%	57%	50%	58%	36%
NPAT	89	92	173	279	409	557
Margin	7%	6%	8%	8%	9%	9%
YoY growth	-23%	4%	88%	61%	47%	36%

Source: Company data, Renaissance Capital estimates

In terms of valuation, international EM peers trade at a median 2016E P/E of 12.5x, on Bloomberg consensus estimates, suggesting to us that Taqa Arabia could be valued in aggregate at EGP3.48bn, translating into EGP1.36 per QH share.

Figure 36: Taqa Arabia peers

		MktCap,$mn	Last price, LC	P/E 2016E, x
RPWR IN Equity	Reliance Power Ltd	2,929	64.1	12.5
EGCO TB Equity	Electricity Generating pcl	2,672	165	10.3
600027 ch Equity	Huadian Power Intl Corp-A	8,480	6.16	9.2
jsw in Equity	JSW Energy Ltd	3,071	114.95	14.2
NOG US Equity	Northern Oil and Gas Inc	416	6.82	24.1
Median				**12.5**

Note: Prices as at 27 January 2015.

Source: Bloomberg

Tawazon

Tawazon is the smallest company in QH's energy portfolio, but it is the largest domestic solid waste management company in Egypt, and possibly the only integrated player in the sector.

The company's operations include the management of waste collection and disposal, as well as the turnkey building of solid waste management facilities. Tawazon also focuses on developing and implementing pro-environment strategies centred on recycling and the creation of alternative fuels, such as biofuels from agricultural waste. Furthermore, the company specialises in producing waste-based products such as animal fodder and compost.

The platform comprises of two distinct entities: 1) Egyptian Company for Solid Waste Recycling (ECARU), which specialises in providing solid waste management services; and (2) Engineering Tasks Group (ENTAG), which is a solid waste management engineering and contracting company.

Through these two companies, Tawazon has previously served clients in Malaysia, Sudan, South Sudan and Libya, and is actively seeking new opportunities in the Gulf cooperation Council (GCC) and the wider Middle East.

Significant beneficiary of changing energy policy

Given the significant changes to industrial energy consumption that are coming with the change in domestic energy policies, we view Tawazon as a way of gaining exposure to energy diversification. The company has already adapted its business model to the new economic reality and signed key contracts with major international firms, such as Italsimenti and Cemex, for the provision of biomass and refuse-derived duel (RDF), which we believe are only going to feature more prominently in industrial energy mix, given the low base and the need for diversification.

The aforementioned contracts link the pricing of the company's biomass and RDF to that of the traditional fossil fuels they partially substitute. The company collects biomass, giving it a significant edge over any other player, and is expanding its processing capabilities of municipal waste and hence RDF. It is investing in increasing the number of processing equipment it owns to be able to maintain its clear first-mover advantage and meet the demand of a quickly growing market for alternative fuel.

The company's near-term plan is to expand to densification technologies in the production of densified pellets and briquettes from biomass. This would allow ECARU to tap the large export market for residential and industrial heating applications. In addition, the company aims to pursue waste-to-electricity applications in the medium-to-long term.

In terms of valuation, although the company is small, it benefits from the high P/E multiples at which peers are trading (17.2x 2016E, on Bloomberg consensus estimates).

Figure 37: Tawazon forecasts, EGPmn (unless otherwise stated)

	2013	2014E	2015E	2016E	2017E
Total revenue	86	187	214	390	562
CoGS	-100	-140	-160	-254	-365
% of revenue	-116%	75%	75%	65%	65%
Gross profit	-14	47	53	137	197
General & administrative expenses	-11	-6	-5	-8	-11
Operating EBITDA	-25	41	48	129	185
EBITDA	-19	33	50	122	177
EBITDA margin	*-22%*	*18%*	*24%*	*31%*	*31%*
EBIT	-28	22	37	97	137
Interest expense	-3	-5	-4	-5	-7
EBT	-31	18	33	92	130
EBT margin	*-36%*	*10%*	*15%*	*24%*	*23%*
Income tax	9	-6	-9	-23	-34
EAT	-22	12	25	69	96
YoY growth		-155%	102%	180%	40%
Net profit margin	*-26%*	*7%*	*11%*	*18%*	*17%*

Source: Company data, Renaissance Capital estimates

Nile Logistics

Nile Logistics is QH's logistics and transportation platform in Egypt and Sudan (including South Sudan). Its key operations are river transport, port management and logistics.

The Egyptian operations include the following.

- **Nile Cargo,** a company that owns and operates a fleet of 70 barges that cover river transport routes from Alexandria to Aswan, and that also provides stevedoring activities in sea ports such as Alexandria and Diametta.

- **National for River Ports Management Company (NRPMC),** a company that owns and operates river ports and warehouses along the entire length of the Nile in Egypt, and whose services are primarily warehousing and stevedoring.

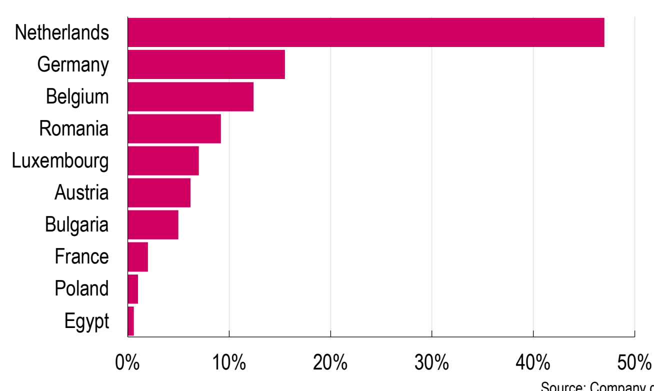
- **Ostool Trucking Company (OTC) Egypt,** where via its minority 28% stake Nile Logistics complements its play on logistics.

In Sudan and South Sudan, Nile Logistics has a small exposure via Nile Barges, a company offering river transport between Juba and Malakal in the South, and NRTC Integrated Solutions, a commercial office selling the services of Nile Barges, in the North. The Sudan and South Sudan operations are momentarily on hold.

River transport – a play on further cuts in subsidies

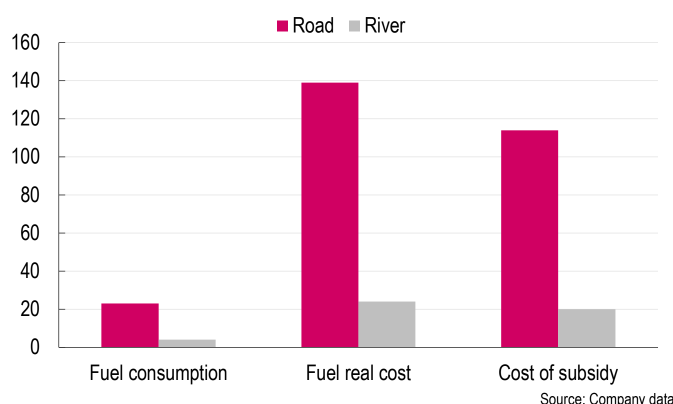
Logistics and transport as a sector accounted for 3.1% of Egypt's GDP in 2013/2014, according to Central Bank data, but river transport accounts for less than 1% of all inland cargo transport, with some 1.3mnt shipped in 2012/13. Owing to fuel price subsidies and a lack of regulation, Egypt's road transportation industry has maintained a virtual monopoly on cargo transport. As the cost of fuel rises and the economics begin to change, we believe cheaper alternatives such as river transport are set to grow in importance. QH management believes that from its current low base, volumes could reach 8-10mn tpa within 8-10 years, suggesting a YoY growth rate of c. 25%.

Figure 38: Market share of river transport in countries with important navigable waterways



Source: Company data

Figure 39: Cost of transport in EGP for 1 tonne-km



Source: Company data

Shift in strategy, as port handling services are more lucrative at current price levels

Despite the c. 75% increase in the price of fuel, margins on current volumes remain too thin for the company to be profitable on this business line alone. We believe further regulation on the road transportation side may be required to kick-start river transport volumes, or more time.

Meanwhile, Nile Cargo and NRPMC are focusing on stevedoring and transhipment as an alternative revenue generator, since margins are higher and demand for their services is high. The companies are now present at all the major Mediterranean and Red Sea ports, and aim to process 2-3mnt in the next 12-18 months, and upwards of 4mn tpa thereafter. While the company initially viewed this segment as a way to use assets and avoid revenue losses, we think it is now a fully-fledged growth area that presents good opportunities for future development.

Medium term, we see coal transportation by river as an opportunity

The change in regulation allowing private coal imports into Egypt will in our view become significant to Nile Logistics' business in the medium term. Should heavy industry make a significant allocation to coal as part of the total energy mix, the most efficient way to transport it will be via river transport. Any outcome will partly depend on legislation and taxes levied on coal and the industries it serves, but we believe coal could easily add 4-5mn tpa to total cargo volumes.

Future synergies with Mashreq, a fuel bunkering facility near the Suez Canal, may also provide upside

QH also owns a subsidiary (Mashreq) with a lease for a 210,000 m2 plot in East Port Said, near the Suez Canal. It aims to develop a state-of-the-art fuel bunkering facility there, and given Nile Logistics' presence in East Port Said and its existing warehousing and stevedoring assets, we believe it is reasonable to expect these companies to use each other's services to maximise their opportunities.

Our assumptions

Our model assumes no operations in Sudan or South Sudan, and the bulk of revenue increases coming from stevedoring and transhipment activities rather than river transport. Given the quick economies of scale achieved in those businesses, we see EBITDA margins rising fairly sharply, although over the longer term they are likely to come down again as river transport takes on more volume.

Figure 40: Nile Logistics summary forecasts, EGPmn (unless otherwise stated)

	2013	2014E	2015E	2016E	2017E
Revenue	45	62	115	184	253
Opex	-61	-63	-52	-74	-88
Gross profits	-14	-1	63	110	164
SG&A	-24	-11	-12	-14	-16
Other adjustments	2	3	3	3	4
EBITDA	-36	-8	32	97	144
Margin	-77%	-13%	28%	53%	57%
EBIT	-129	-50	-11	47	87
Net interest	-44	-60	-42	-41	-67
EBT	-178	10	-53	7	19
Taxes	0	-1	-3	-3	-4
EAT	-185	-98	-51	9	21

Source: Company data, Renaissance Capital estimates

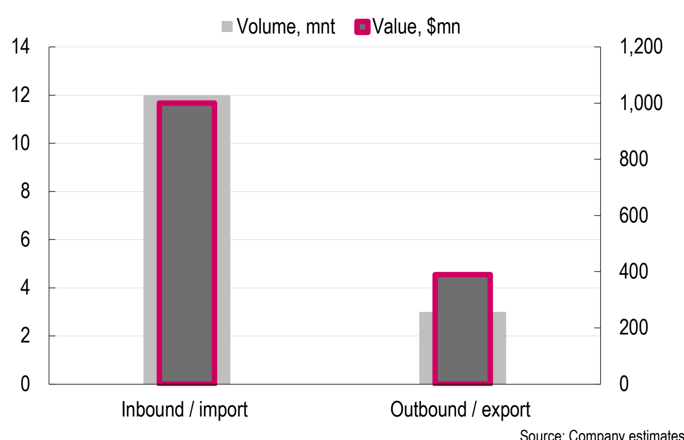
With a peer group trading at 15.0x 2016E earnings, on Bloomberg consensus estimates, we think this company could be valued at EGP135mn. However, we think the real value could be much higher, since 2016E represents the first year of true profitability for us; we believe a P/E based on 2017E is likely to be a better yardstick of actual value (but we still use 2016E in our valuation).

Africa Railways

This asset represents QH's foray into African railways, and currently the main investment is a controlling 30% stake in Rift Valley Railways (RVR), which has a 25-year concession to operate railways in Kenya and Uganda. This is a c. 2,400-km network that links the port of Mombasa to inland Kenya and Uganda, and represents exposure to the port of Mombasa's rising volumes and deep competitive advantage of rail vs trucking.

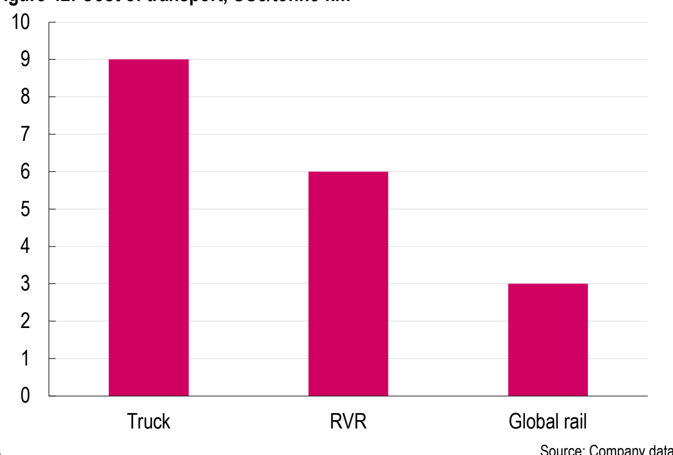
QH estimates that import volumes through the port of Mombasa and inland into Kenya and Uganda are in the order of 12mn tpa, with a transport value of c. $1bn. On the export side, QH estimates volumes at c. 4mn tpa for a transport value of c. $390mn. Currently the vast majority of cargo is transported by truck, where tonne-km prices are around USc9. We believe RVR could cut this cost by one-third, with further gains to be had from investments to reach the global cost of USc3/tonne-km.

Figure 41: Import and export volumes and values



Source: Company estimates

Figure 42: Cost of transport, USc/tonne-km



Source: Company data

The company's medium-term goal is to capture c. 15% market share by rail by improving safety, reliability and operational efficiency in phase one, and adding new locomotives and wagons in phase two of a five-year turnaround programme. The company began phase two in 2014. The turnaround programme is fully funded in the amount of $300mn.

Key near-term issues we see are the acquisition of new locomotives and wagons, improving efficiencies and converting more customers. The company recently signed up a number of new clients, including Total, Vivo (formerly Shell Africa) and Roofings Group; the largest steel fabricator in Uganda.

Figure 43: Africa Rail forecasts, $mn (unless otherwise stated)

	FY13	FY14	FY15E	FY16E	FY17E
Revenue	62.1	87.3	132.9	175.3	219.6
Direct cost	20.1	39.3	50.5	66.6	61.8
Operating expenses	39.3	40.0	45.0	48.0	45.1
Operating EBITDA	-2.1	-1.5	25.7	49.0	97.9
EBITDA margin	-3.4%	-1.7%	19.3%	28.0%	44.6%
EGP/$	7.15	7.15	7.8	8.0	8.0
Revenue, EGPmn	443.7	624.4	1,036.3	1,402.3	1,757.1
EBITDA, EGPmn	-14.9	-10.5	200.2	392.0	783.1
Net income, EGPmn	(190.26)	(85.80)	(7.80)	29.45	40.80

Source: Company data, Renaissance Capital estimates

In terms of valuation, we use a peer group that is similar to the one we use for Nile Logistics, since both are in essence logistics providers. At 15.2x 2015E estimated earnings, we value the company at EGP448mn.

Other assets

QH owns more assets than we cover in our report, as we lack sufficient clarity to derive credible valuations. Some of these belong in the firm's core portfolio, and we provide only a brief description.

Mashreq (acquired 2009)

This is a greenfield project that aims to leverage the high-bulk shipment volumes transiting the Suez Canal by providing specialised services in oil product bunkering and storage. This company was initially part of the Taqa Arabia portfolio (acquired by Taqa Arabia in 2007) but was later spun off to Citadel Capital.

Mashreq has signed a concession agreement with the East Port Said Authority allowing it to build a first-of-its-kind independent tank terminal, to provide storage for liquid bulk petroleum products and bunkering/blending services. This is a 30-year concession (with provisions to extend) that is based on a build-operate-transfer (BOT) system. It is not currently in operation; QH has stated that it is negotiating with third parties to partner on the venture.

Gozour and Wafra (2007)

These companies form an integrated agri-food group operating in agricultural farmland and dairy products and in fast moving consumer goods (FMCG). It owns prime farmland near Cairo, called Dina Farms. This is the largest private farm in Egypt (40mn km2), and with c. 16,000 cattle (of which c. 7,500 are milking cows) it is the largest producer of raw milk in Egypt (capacity c. 70k tpa). Farm products are marketed through a fast-growing network of retail outlets, with annual turnover of >EGP100m. On the FMCG side, Gozour owns three major local brands: Rashidi el Mizan, which makes confectionary and jams; Enjoy, which is the second-largest dairy and juice brand in Egypt; and Elmisrieen, which is a popular local cheese manufacturer.

Gozour and Wafra were acquired by Citadel Capital in 2007 and have been built up through consolidations. They provide exposure to the macro environment in terms of consumption trends into higher-value and better-quality food segments. Gozour is active in Egypt and Sudan.

Wafra is an agricultural production company operating in Sudan and South Sudan, with rights to large land plots. The civil conflict in South Sudan is having an impact on operations, but some grain sorghum and maize have been planted and harvested (nearly 200 tonnes in total). Activities in Sudan are on hold owing to soil testing being carried out; in the meantime the company is using its machinery to work for third parties.

Ascom (2006)

Ascom is QH's investment in the mining segment. It has three key business segments: quarry management and services; mining; and manufacturing. Activities are mainly in Egypt, but increasingly in MENA. This is a listed company with a market cap of c. $60mn. Revenue in FY13 was $75.2mn.

In quarry management and services, Ascom is a leading supplier of limestone, clay, silica and gypsum. It currently supplies >40% of the cement market in Egypt. In manufacturing, we believe Ascom is well positioned to leverage the high-quality calcium carbonate found in Egypt through a greenfield factory in Upper Egypt, which we think should double its current milling capacity of 120,000 tonnes. The company is also developing capacity in glass wool and rock wool, both of which have strong export prospects, in our view.

In mining, Ascom has several concessions in Sudan and Ethiopia that it uses for the exploration of gold, silver and copper. Gold has been discovered in Ethiopia; the company recently released its maiden mineral resource estimate (1.7mn oz at 1.5 grammes/tonne).

Ascom is further expanding its scope to offer mining of building materials. It also mines aggregates, armoured blocks, gravel, silica sand and kaolin in Egypt and Algeria.

Potential new projects include building a DAP plant with capacity of 1mn tpa, geared mostly to export markets, and a lime plant with capacity of 200-250k tpa.

Ascom has been approved by the Egyptian Army as a supplier for the new Suez Canal (dry sand excavation).

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