

Qalaa Holdings (QH)

Overweight

Quest for value

- It gets much more interesting for QH in 2015 and beyond, with operations at its Egyptian cement plant and as energy investments pay-off strongly
- Leverage does not concern us: i) 2015e EBITDA-to-interest is 1.5x, ii) 2017e free cash flow yields grow to 30% and, iii) if QH exits non-core holdings, it could substantially de-lever
- Initiate at Overweight with a TP of EGP4.9/share. The end of the lock-up period may provide a better entry point

The tables have turned for Qalaa Holdings (QH)—top-down, Egypt started reforming energy subsidies, the premise for its core investments. Bottom-up, transformation is in progress with QH closing an EGP3.64bn capital increase, raising its ownership in holdings via a series of swaps, in addition to delivering on its strategy to exit non-core holdings. We expect 2016 EBITDA to stand 2.5x higher than 2014e, driven by full operations at its strategically located 2mn tpa Egyptian cement plant, due for coal conversion by May 2015 and for brownfield expansion by 2017. We also expect integrated energy investments to pay-off strongly. By 2016, QH will have emerged into a holding company that consists of two main business lines: cement (57% of 2016e EBITDA) and energy (24%)—together representing c90% of our SoTP value. QH's 4.7mn tpa greenfield refinery, Egyptian Refinery Company (ERC), is slated to begin operations in 2017 and alone boost EBITDA by a further EGP3.7bn, and an even higher EGP5.4bn once fully operational in 2018 to a consolidated figure of EGP8.2bn, implying a sustainable yearly free cash flow of EGP1/share, a yield of c30% on current share price levels. Announcement of a partnership agreement at Mashreq (30-year concession for fuel storage and bunkering services at the Suez Canal) could add EGP500mn in annual EBITDA to our forecasts.

QH's leverage does not concern us; shares should rerate further with ERC. We expect QH's 2015e EBITDA to cover interest by 1.5x, as we are bullish on EBITDA growth and as the bulk of debt relates to QH's refinery greenfield, where interest costs are capitalised. ERC's construction is now over 40% complete and as its start date approaches, we expect QH shares to rerate further as it should add c60% to 2017 group EBITDA, narrowing the conglomerate discount and as comparable refineries trade at 6-7x EV/EBITDA. If QH generates the guided EGP3.1bn as proceeds (net of bank dues) from non-core asset sales, it would be able to enjoy a net cash position, ex ERC project financing.

Initiate at Overweight. QH presents an opportunity to buy an undervalued company in transformation with a 2017e EV/EBITDA multiple of 4.0x and P/E multiple of 4.6x. However, although its market cap is down by c30% in the last six months, we note that 37.6% of QH's free float is locked-up from last year's swap until 16 April. Because there is no precise way to determine the extent of a potential overhang, we opt to be buyers after lock-up expiry. Risks include a higher-than-assumed conglomerate discount assigned to the stock, and the necessity of a more substantial earnings recovery to price-in fundamentals; QH will only start generating profits in 3Q15 and any write-downs from underperforming non-core assets beyond 3Q could push the earnings recovery story further out.

KPI summary

Dec EGPmn	2013 ¹	2014e	2015e	2016e	2017e	2018e
Revenue	4,806	6,386	8,867	10,997	27,175	36,314
EBITDA	(85)	651	1,118	1,636	5,984	8,165
EBITDA growth (% y-o-y)	n/m	n/m	72	46	266	36
Net income	(786)	(595)	(21)	284	1,189	1,652
P/E (x)	n/m	n/m	n/m	19.1	4.6	3.3
Net debt/EBITDA (x)	n/m	22.0	17.4	13.5	3.4	2.1
EBITDA/interest (x)	n/m	0.8	1.5	2.4	6.4	6.3

Source: QH, CI Capital estimates. Note (1): based on proforma financials.

Target price (EGP)	4.90
Share price (EGP)	2.87
Potential return (%)	70.7

Share details

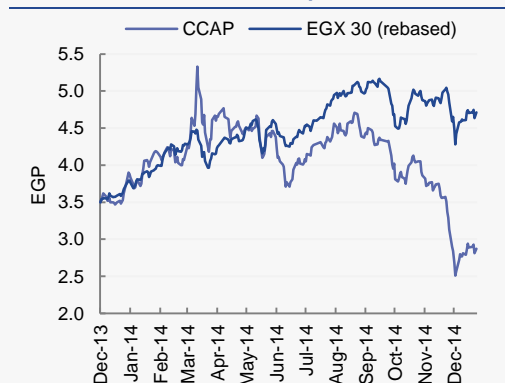
Ticker	CCAP EY / CCAP.CA
12M avg daily value (USDmn)	4.7
% Δ: m-o-m / 6M / y-o-y	(18.2) / (29.7) / (18.7)
No. of shares / float (mn)	1,600 / 883
Market cap (EGPmn)	3,444
Market cap (USDmn)	482

Ownership structure

Citadel Capital Partners (CCP) ¹	27.6%
Suleiman Abanumay	7.2%
EIIC	10.0%
Free float ²	55.2%

Source: QH, Bloomberg. Note (1): CCP is owned by management of QH; Shares are preferred shares, with each preferred share having the voting power of 3 ordinary shares, providing CCP the ability to maintain control. Note (2): Includes 331.6mn of shares in lock-up till 16 April 2015.

Absolute and relative share performance



Source: Bloomberg
Prices as of 8 January 2015

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Investment case and valuation

- Our preferred divisions—cement and energy—offer substantial EBITDA growth, 10.8x over 2014-18e; we see the blended RoE on QH’s core assets at 20%, with partnerships at Mashreq providing upside
- QH is loss-making today as its investment ideas were early-cycle, but the backdrop is conducive for these investments to generate substantial growth
- Initiate at Overweight as a value play, trading on PE multiples of 4.6x and 3.3x in 2017e and 2018e, respectively; optimisation of QH’s book via non-core asset exits should act as a catalyst by unlocking value and de-levering

Background on Qalaa Holdings (QH)

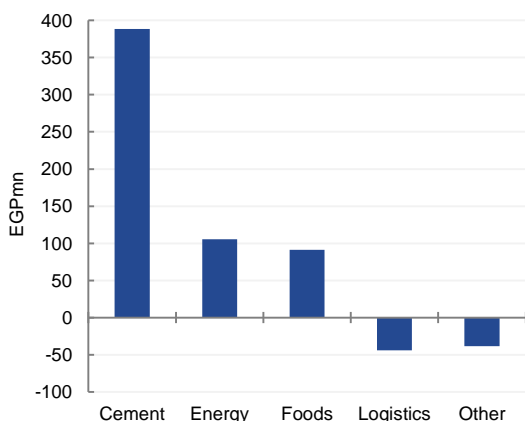
QH has started implementing its strategy of shifting from a private equity firm to a holding company that focuses on investments in cement, energy, transport and logistics, food, and mining. Although it has a multitude of other holdings, together these five units generate the company’s EBITDA—cement currently being the largest, at c77% of 9M14 EBITDA (from continuing operations). Its recent history has been turbulent, having faced red tape in Algeria, as well as political instability in Iraq and Syria, within its cement portfolio. Also, in Egypt, the 2011 revolution delayed receipt of land on which QH’s refinery (USD3.7bn project) was to be built. As a result of this turbulence, and the investments’ long-term nature, QH founders had supported the decision to transform the firm into an investment holding company. Management decided to adopt what we regard as a notably more focused investment strategy that, in our view, will serially reduce the conglomerate discount assigned to the stock. Among QH’s five key divisions, we focus on cement, energy, and transport, which we believe, will drive the lion’s share of future growth.

Cement [77% of 9M14 EBITDA]—will be the main contributor to consolidated EBITDA through to 2016. This division consists of a new 2mn tpa cement plant in the South of Egypt (Minya), a 1.62mn tpa cement plant in North Sudan—both fully-integrated, a 27.55% equity stake in Misr Cement-Qena [MCQE EY | Overweight | TP EGP135], a 2mn tpa cement plant in Upper Egypt, in addition to a ready-mix business specialised in cement industry engineering and plant maintenance services.

Energy [21% of 9M14 EBITDA]—is Egypt’s largest private sector energy distribution platform, with activities ranging from gas network contracting to distribution, electricity generation and distribution, and fuel marketing. This division also has an ongoing greenfield refinery project that should supply Egypt with 4.7mn tpa of strategic fuels as of 2017, currently being imported. Added to that is the fact that the Egyptian public sector is among QH’s partners in the project, which to us indicates that the project carries low operating risks.

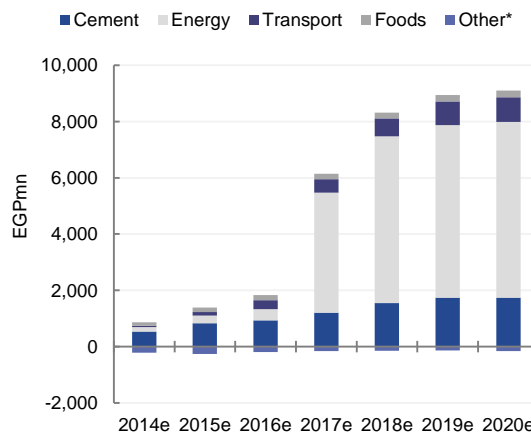
Transport [-9% of 9M14 EBITDA]—Although it remains loss-making, we believe this unit carries strong growth prospects, mainly thanks to a 25-year concession to operate 2,352km of track connecting the Indian Ocean port of Mombasa in Kenya to the centers of both Kenya and Uganda, two countries that currently have no other railway operators. The concession reversed 2013 losses of EGP26mn last year and should generate EGP850mn of yearly EBITDA by 2020.

9M14 consolidated EBITDA (from continuing operations) split by division



Source: QH

Consolidated EBITDA (from continuing operations) will evolve sharply going forward



Source: CI Capital estimates

Positively exposed to Egypt's power market reform

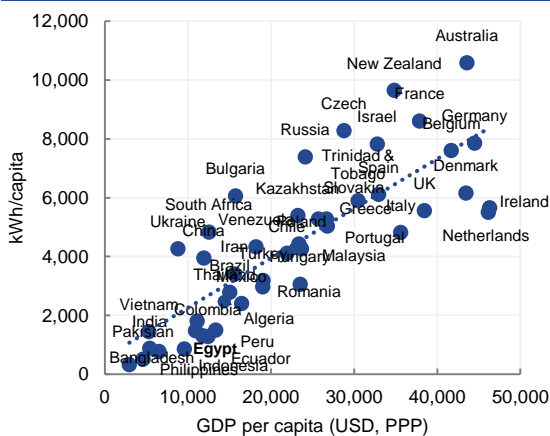
High increases in Egypt's electricity demand of 7% p.a. (and higher increases in peak demand of 11% p.a. lead by the household sector), as power remains heavily subsidised, means that substantial investments are now required. The government has begun addressing the fact that tariffs were less than the economic cost, raising electricity prices in July 2014, and more importantly committing to liberalise power prices in five years' time. The magnitude of the July 2014 increase (15-66% depending on consumption bracket), the approval to use coal as a source of fuel in power generation, alongside other reform measures taken to date (outlined below) is unprecedented. As a result, we are bullish on the government's USD23bn power project spending pipeline (2015-17). This is equivalent to 3.7x the power projects currently underway and is separate to private sector industrial sector initiatives to ensure captive power supply and avoid disruptions. Nationwide, there is an estimated 32,000 MW of new capacity needed by 2020. QH's power generation and distribution company (a c40% gross margin business) stands to benefit greatly from such reforms. We note here that two of QH's energy units have robust cash generation abilities with working capital throwing cash equivalent to 15% of sales on a yearly basis.

Egyptian Electricity Holding Company (EEHC) owns c90% of generation, 100% of transmission and c99% of distribution

	Current market	Potential
Generation: Public (90%)	Public: 6 generation companies, 27 GW production capacity Private: Three 20-year BOOT contracts with 2 GW, with all output sold directly to Egyptian Electric Transmission Co. (EETC)	Jul 2014 power price increases (by a blended 50% vs. historical average of 5% pa) and plan to liberalise power prices by 2019 should encourage both public and private generation investment Self- and co-generation, feed-in-tariff, and the approval to use coal should also spur investment in generation as oil/gas availability was previously a concern Private generation companies will have the right to conclude direct bilateral contracts with clients
Transmission: Public (100%)	Public: EETC is the sole transmission entity, purchasing all output from generation plants	Establishment of Transmission System Operator to provide assurance of its independence and full unbundling from the rest of the power supply chain There are no plans to allow private sector participation in transmission
Distribution: Public (99%)	Public: 9 public companies, purchase power from EETC to 28mn customers Private: 15 private electricity distributors are licensed, with Taqa Arabia claiming it is the largest private player	The government is introducing reform to allow direct, bilateral agreements between private producers and end users By introduction competition, those with better efficiency and services should fare better

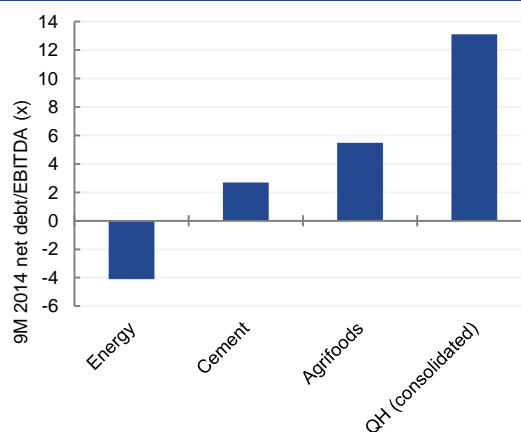
Source: Ministry of Electricity, CI Capital Research

Egypt on electricity generation per capita vs. GDP per capita



Source: BP Statistical Review, World Bank

QH's energy unit is cash rich and generative, with working capital throwing 15% of sales as cash



Source: QH. Note: Energy division excludes EGP3.5bn debt related to QH's greenfield refinery project and Cement and QH consolidated figures exclude convertible debt.

ERC enjoys unique footing

The Egyptian government has high interest in ERC's launch

ERC should address the growing supply-demand imbalance in Egypt's refined oil products market, decreasing dependency on select petroleum imports by c50% when fully operational. The Egyptian government, via EGPC (Egyptian General Petroleum Company), owns a 23.8% stake in the project, and so its interests are aligned with QH's, if not higher given: 1) EGPC expects there to be annual cost savings of cUSD300mn through avoided transportation and insurance costs, eliminated product shipment losses, and generated revenues through the storage and processing fees; ERC will enjoy a strategic location close to main consumers in Cairo and Upper Egypt, which represent 65% and 44% of total fuel oil and diesel demand, 2) it will add 13% to the country's refining capacity, 3) it will improve the age of the industry, which is currently older than 50 years of age.

ERC vs. Egypt's oil refining industry: 9 refineries, 5 main locations

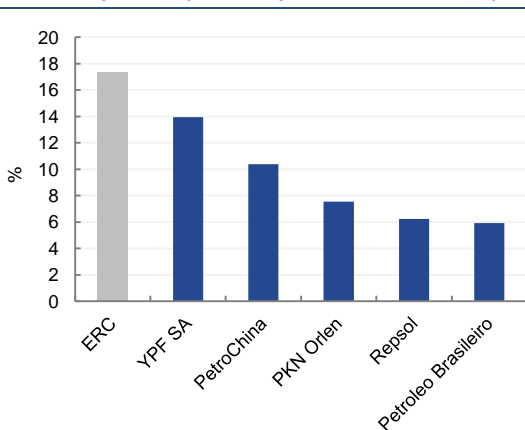
Refinery	Start-up	Location	Capacity (b/d)	% of total refining capacity
AMOC	2002	Alexandria	34,447	4
MIDOR	2001	Alexandria	100,000	13
Asyut	1987	Asyut	47,000	6
Tanta	1973	Tanta	35,000	5
Ameriya	1972	Alexandria	78,000	10
Cairo Oil (CORC)	1969	Cairo	160,000	21
Alexandria	1957	Alexandria	100,000	13
El Suez	1921	Suez	66,400	9
El Nasr	1913	Suez	146,300	19
Total			767,147	
ERC	2018	Cairo	97,489	13

Source: ERC, CI Capital Research

Favourable refinery economics thanks to supply and product off-takes

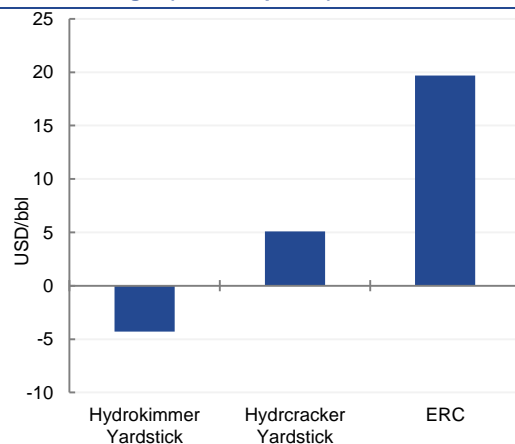
ERC is designed to produce over 4.6mn tpa of refined products, including 2.3mn tpa of diesel for vehicle usage, in line with Euro V standards, a very-high quality fuel that follows European emission standards. The sale of ERC's refined products to the state-owned EGPC will be implemented through an offtake agreement on a 'take or pay' basis in USD, based on international product prices. The signed agreement states that the EGPC and its affiliates are committed, through a 25-year feedstock supply contract, from the first day of ERC's commercial operations to i) supply and deliver ERC a minimum of 3.5mn tpa of atmospheric residue at Mediterranean high sulphur fuel oil prices plus a 4.4% premium, as well as ii) provide additional quantities of atmospheric residue to ERC on a priority basis. Construction of ERC is c40% complete and given the investment has a very sound footing as its start date approaches, we expect QH shares to rerate further (comparable refineries trade at 6-7x EV/EBITDA, noting that we expect ERC to generate a superior RoE of 17% vs. a peer average of 10%), but also given the conglomerate discount on the stock is likely to narrow; By 2018 we estimate ERC's contribution to group EBITDA c60%, putting the stock on an EV/EBITDA multiple of 4.0x and P/E multiple of 4.6x. Now ERC is contributing 53% to group net debt.

RoE comparison (2014 for peers, 2020e for ERC)



Source: Bloomberg, CI Capital estimates

2020 net margin (2011 PG prices)



Source: Purvin & Gertz, ERC, QH

We also like QH's Egyptian cement holdings, as we are bullish on the market

Close to 80% of industry players have plans to migrate away from state-provisioned fuel to coal and alternative fuels, due to supply shortages and subsidy reductions, and despite the low visibility on the coal legislation currently in the works. Migration would allow full capacity utilisation and improve EBITDA margins by an average EGP47/t (USD6.6/t), or 30%. If the government continues to increase fuel prices as we expect it to, migration savings would improve margins by cEGP20/t (USD2.8/t) for every USD1/mmBtu hike. Our positive outlook is despite us assuming a 30% tax on landed coal costs effective January 2015, which would necessitate a marginal c3.5% price increase to pass through, all else constant.

We believe the market's apparent concerns about the rise in supply, as the sector converts to coal, are exaggerated. On our calculations, 2015-17 will see growth in consumption improving operating rates and pricing, driven by pent-up demand for private housing, improved confidence, and inflation hedging, in addition to construction demand from the reinstatement of suspended projects and FDIs, particularly in the infrastructure space. The government has proven its drive to upgrade the country's infrastructure, having awarded USD20bn's worth of projects in 2H14 alone, 70% of which is funded off the government's balance sheet. With construction demand expected to come in at 5% of real GDP, cement consumption should grow by an average 8.2% a year over 2015 and 2016 vs. 1.8% y-o-y in 2014. While the industry is likely to see new brownfield supply, given the availability of new energy sources (QH's plant, Minya Cement is among those adding supply: 1.4mn tpa up to 3.4mn tpa), this is a story for 2017 and beyond, and at current prices, a typical brownfield project would generate a negative IRR, supporting our view of price growth ahead.

Industry assumptions

	2011	2012	2013e	2014e	2015e	2016e	2017e
Capacity (mn t)	59.1	62.4	66.6	67.4	69.2	70.8	73.9
Capacity utilisation (%)	82.5	84.7	77.0	74.3	79.3	88.4	97.9
Production (mn t)	48.7	52.9	51.3	50.1	54.3	62.0	71.8
Domestic sales (mn t)	48.1	51.5	49.9	50.7	55.8	60.7	67.7
Imports (mn t)	0.5	0.0	-	0.1	0.9	-	-
Consumption (mn t)	48.6	51.5	49.9	50.8	56.7	60.7	67.7
Net exports / imports (mn t)	0.2	2.0	0.2	(0.1)	(0.9)	1.8	4.6
Local price (ex-factory, EGP/t)	380	420	550	675	707	744	810

Source: Ministry of Industry and Trade, Ministry of Planning, CAPMAS, CI Capital estimates

A closer look at QH's leverage

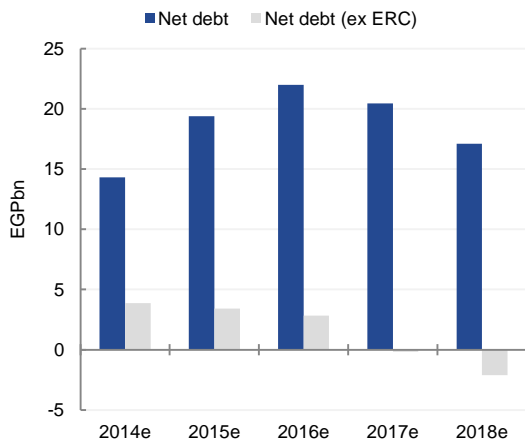
While we expect QH to closed Sep-14 with leverage of EGP11.7bn, we are not concerned, seeing that QH's 2015e and 2016e EBITDA should cover interest 1.5x and 2.4x respectively, as we are bullish on EBITDA growth and as the bulk of debt relates to the company's refinery greenfield, where interest costs are capitalised. There is upside to our EBITDA estimates should the company seal partnerships at 54.9%-owned Mashreq (a 30-year concession for fuel storage and bunkering services at the Suez Canal), which could add EGP500mn in annual EBITDA. Also, we note that proceeds from AFS assets, planned to be divested over the coming c4 years, could help de-lever, reducing net debt/EBITDA at a faster rate. The company is guiding for aggregate proceeds net of bank dues of EGP3.1bn, which would lower 2015e net debt by 16% or a notable 90% excluding ERC project debt. With the exception of the company's Algerian cement assets (two plants with a capacity of 6.1mn tpa), the company's AFS asset portfolio is relatively diversified, as shown below, increasing the likelihood of divestitures.

Overview of QH's non-core asset portfolio up for sale (book values as of Sep-14, proportionate to QH ownership)

Sector	No. of companies	Book value (EGPmn)	BV (EGP per share)	% of non-core asset portfolio	% of QH book
Algeria cement assets	1	874	0.55	55	20
Speciality real estate	1	279	0.17	18	6
Upstream oil & gas	3	166	0.10	10	4
Investment funds	2	150	0.09	9	3
Financial services	1	116	0.07	7	3
Total		1,585	0.99	100	36

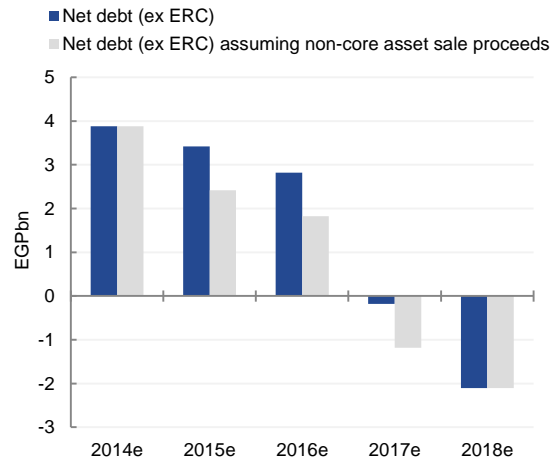
Source: QH, CI Capital estimates

The bulk of QH's net debt pertains to its greenfield refinery



Source: CI Capital estimates

QH's net debt profile would improve greatly if it stacks up to guidance on sale proceeds



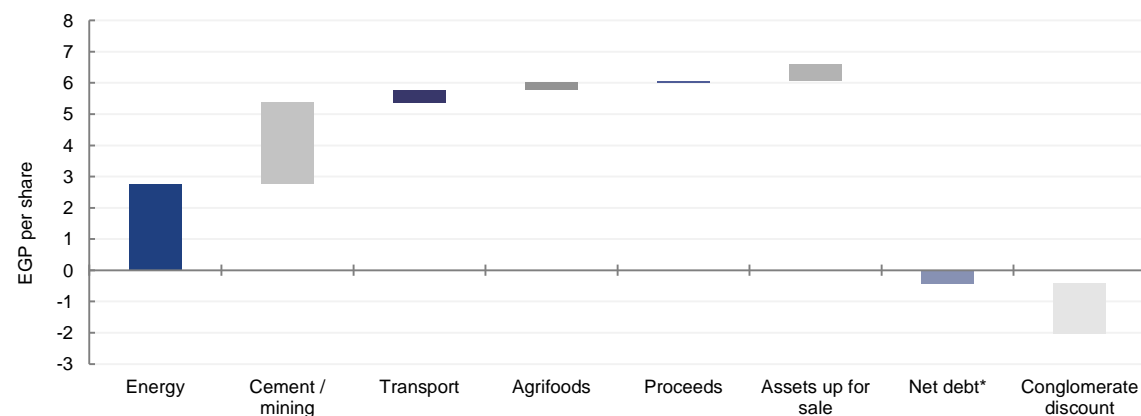
Source: CI Capital estimates

Valuation

We value QH on a sum-of-the-parts basis, using various valuation methodologies for its core holdings, and assigning a blended average price to book multiple of 0.53x for its non-core holdings based on a 0.4x multiple for the company's Algerian cement assets, to factor in higher uncertainty over their valuation given associated political risks and 0.7x for the remaining AFS assets, which are mostly Egypt-centric property investments and financial sector investments. We then assign a 20% discount to the sum of the parts valuation for QH of EGP6.12/share to reflect the company's conglomerate structure, leaving us with a target price of EGP4.90/share. As our target price implies potential return of 70.7% to the 8 January 2015 closing price, we initiate coverage of QH with an Overweight rating. Our valuation post the assumed conglomerate discount is equivalent to 1.8x the value of the company's book as of September 2014.

Altogether, cement and energy represent the largest contributions, each approximately 44% of our SoTP TP. The single largest entity contributing to our target price is ASEC Holding, alone 29% of our SoTP value, or EGP1.79/share. We value this entity using DCF, and the value we reach implies an EV of USD220/t, relatively in line with CI Capital valuations for rated cement stocks in comparable locations in the South of Egypt. The second largest entity is Taqa Arabia at 26% of our SoTP value (EGP1.57/share), for which our valuation implies a price-to-book multiple of 4.1x, justified in our view by this business model's healthy cash generation capability. Both these assets which, in our view, carry low operational risks are together worth EGP3.36/share, which stands higher than the current share price, even after deducting net debt at the parent company.

QH SoTP valuation breakdown by division



Source: CI Capital estimates

Note *: at parent level which is otherwise unaccounted for.

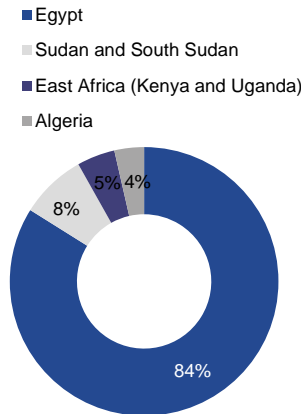
Sum of the parts valuation summary for QH

	Ownership (%)	Valuation methodology	Total		Proportionate		TP	
			EV (EGPmn)	Equity (EGPmn)	EV (EGPmn)	Equity (EGPmn)	(EGP/share)	% of TP
Energy								45
Taqa Arabia	62.5	DCF	3,661	4,019	2,288	2,512	1.57	26
ERC	15.2	DCF	14,409	11,056	2,190	1,680	1.05	17
Tawazon	47.9	DCF	327	332	157	159	0.10	2
Mashreq ¹	54.9	1x P/BV	106	123	51	68	0.04	1
Cement & mining								43
ASEC Holding (ex MCQ)	69.2	DCF	7,492	4,145	5,185	2,868	1.79	29
Misr Cement-Qena (MCQ) ²	27.6	DCF	2,963	3,540	816	975	0.61	10
ASEC Cement (direct)	4.9	8x 2015e EV/EBITDA	5,484	3,984	266	193	0.12	2
ASCOM	39.2	At market price	977	380	383	149	0.09	2
Transport								7
Africa Railways	30.8	DCF	2,467	1,453	760	447	0.28	5
Nile Logistics	62.0	DCF	841	314	522	195	0.12	2
Agrifoods								4
Gozour ³	43.1	15x 2015e P/E	751	648	324	279	0.17	3
Wafra ⁴	100	0.5x P/BV	53	93	53	93	0.06	1
Subtotal for core units							6.01	98
Algerian cement assets for sale	n/a	0.4x P/B				874	0.22	
Diversified assets up for sale ⁵	n/a	0.7x P/B				711	0.31	
Subtotal for non-core units							0.53	9
Proceeds from sales post 3Q14		DCF				103	0.06	
Cash		Sep-14				233	0.15	
Debt		Sep-14				1,015	(0.63)	
Net debt at parent, unaccounted for							(0.42)	(7)
QH SoTP							6.12	
Conglomerate discount (%)							20.0	
QH SoTP target price							4.90	

Source: CI Capital estimates

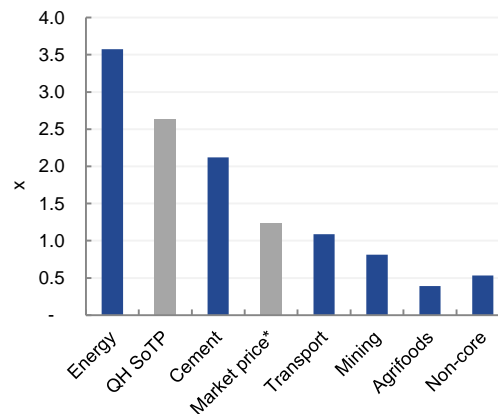
Note (1): QH is currently involved in non-exclusive negotiations regarding potential partnerships to build and operate the storage and bunkering terminal at Mashreq. While the company expects to generate sustainable revenue of USD135mn and EBITDA of USD80mn from Mashreq, we choose to value the project at book, primarily to reflect the historical costs of land, unless the company begins construction. Note (2): Based on CI capital valuation for Misr Cement-Qena [MCQE EY | Overweight | TP EGP135/share]. Note (3): operates Egypt's largest private farm (40mn sqm) producing 63k tpa of milk in addition to other foods, a retail business which markets the farm's produce to A and B+ customers with a target to double its branch network to 30 stores by 2020, covering 65k sqm of retail space. Gozour remained loss-making as of Sep-14, but we expect the company to turn profitable in 2015. Note (4): c500k acres in Sudan and South Sudan with full water rights under a 25-year lease to serve local demand. The entity was loss-making as of Sep-14 and given our negative outlook on global grain prices, with stocks at 25% of global production as per UN data, we do not expect Wafra will turn profitable over our forecast period. Note (5): includes Tanmeyah, the company's micro-financing business, which is classified as non-core long-term non-core by QH.

QH valuation split by geography (pre conglomerate discount)



Source: CI Capital estimates

P/B implied by our valuation per segment (pre conglomerate discount)



Source: CI Capital estimates
Note *: based on the equity value for QH of EGP3.4/share

Risks

Changes in government policy, or lack of follow-through; any new major company ventures

QH's three core segments, energy and cement, benefit greatly from the newly elected regime's policies. Our growth assumptions for QH's energy business would be negatively affected if there is a change in or lack of follow-through on energy subsidy reform. For QH's cement division, the key risks would be if the government charges a higher-than-expected coal tax (we assume 30% on landed coal costs), or government intervention in pricing. Also, any change in strategy at the company-level, such as another large equity investment in a new sector, may in our view be unwelcomed by the market as it would not only further delay the company's positive free cash generation, but also reduce credibility of management who have more recently communicated a strategy of lessening diversification.

Overhang as the lock-up expires on 16 April 2015

During 1Q14, QH completed an EGP3.6bn capital increase by issuing approximately 0.7mn new shares at par value. This was a non-cash transaction, as the issued shares allowed holders of platform companies to swap their shares into QH shares. Out of the issued shares, 331.6mn are locked up until 16 April 2015. This is equivalent to nearly 37% of the stock's free float and so could present an overhang if sold unorderly. There is no precise way to determine the extent to which there could be an overhang on the stock from holders looking to cash their shares, as this depends on whether each of the various shareholders' target for returns. We do note, however, that according to QH, c220mn shares of the 331.6mn locked up are held by QH shareholders, leaving a lower amount (the remaining 111.6mn shares) as those more likely to be sold. QH is planning a second swap in May 2015 (c400mn shares, also at par), to raise its stakes across its holdings.

QH ownership of core and non-core subsidiaries pre and post share swap

	Pre swap (%)	Current (%)	Stake purchased (%)	
Core	Taqa Arabia	33.8	62.5	28.7
	Tawazon	47.9	47.9	0
	ERC	11.7	15.2	3.5
	Mashreq	34.4	54.9	20.5
	Nile Logistics	37.9	62.0	24.1
	Africa Railways	28.2	30.8	2.6
	Gozour	20.0	43.1	23.1
	Wafra	100	100	0
	Ascom	39.2	39.2	0
	ASEC Holding	54.8	69.2	14.4
Non-core	Glassworks	21.0	47.6	26.6
	United Foundaries	30.0	67.4	37.4
	Finance Unlimited	99.9	99.9	0
	Bonyan	32.1	60.2	28.1
	Grandview	13.0	42.8	29.8

Source: QH

Unfavourable surprises from QH's non-core assets

We calculate that QH's non-core assets constitute a total of EGP0.99/share at book, of which c45% is diversely split between multi-sector assets, mostly in Egypt, and c55% is the company's disputed Algerian cement assets, which it committed to sell in May 2014. The necessity of a more substantial earnings recovery to price-in fundamentals (QH will only start to generate profits in 3Q15) could be an overhang on the stock, and any writedowns from loss-making non-core assets, which are only targeted for sale over a three- to five-year timeframe, could push the earnings recovery further out. We would be particularly concerned over Algerian cement assets, since they are more sizeable and given the April 2014 reelection of President Abdelaziz Bouteflika that reaffirmed the country's anti-investment policies. One caveat to this argument could be that Algerian policies adjust to the new norm of lower oil prices. On 8 January 2015, OPEC member Algeria, announced that its foreign exchange reserves dropped by USD8bn in 3Q14, a 4.3% decline from Jun-2014 levels. Although foreign reserves remain substantial at USD185bn (vs. foreign debt of USD3.7bn), the country could introduce pro-foreign investment policies as its budget would fall into deficit otherwise. Based on IMF estimates, 2014 would be the first year for Algeria to record a fiscal deficit since 1999. Any resolution of QH's Algerian cement assets could instigate sale, and likely at a more attractive deal price too.

Management fees could deter investors for corporate governance reasons

An EGM in May 2008 approved the management contract with Citadel Capital Partners (CCP), QH's leading shareholder, and the company's board majority, which states that CCP provides management duties for fees based on 10% of the annual standalone net profit available for distribution. This agreement shall remain in effect as long as CCP owns 15% or more preferred shares. CCP consists of four individuals, who are members of the firm's executive committee.

An overview of QH's three main core divisions

Energy
Cement
Transport

Energy [45% of SoTP valuation]

- QH's operative energy businesses are uniquely cash-rich and cash-generative
- We expect robust growth in light of Egypt's unprecedented energy policy reforms, particularly within the electricity market
- ERC's launch in mid-2017 should help rerate QH shares, reducing the conglomerate discount assigned to the stock, since it will contribute c60% of group EBITDA

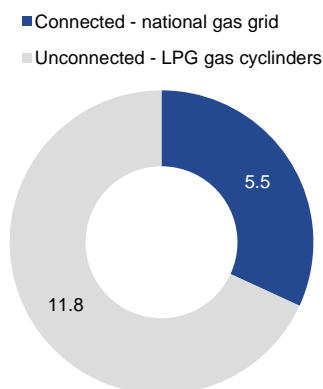
Taqa Arabia

Taqa Arabia (62.5%-owned) is the largest private sector energy distribution company in Egypt, with activities ranging from gas network contracting to electricity generation, distribution, and fuel marketing. Taqa provides services through four lines of business, namely Taqa Gas, Taqa Power, Taqa EPC, and Taqa Marketing. The company is strategically positioned to capitalise on opportunities as increased energy demands place further strain on the national grid and as the government reforms the power market to accommodate for private-sector involvement in the upgrade of the country's generation capacity.

Taqa Gas (33% Taqa Arabia's 2013 gross profit) and Taqa EPC (13%): Taqa Arabia's gas distribution arm has licenses for natural gas operation, maintenance and distribution via four concessions—City Gas, Repco Gas, Nile Valley Gas, and Trans Gas—across 11 Egyptian governorates. There are a total of 13 local distribution companies (LDC) in Egypt, including Taqa Gas's; of the others, four are owned by the state and five by the private sector—mainly by Natenergy, which is wholly-owned by EK Holding [EKHO EY | Neutral | TP USD1.0]. The company's natural gas distribution peaked at c5.4bn cbm in 2012, accounting for 55% of the private LDC market. In Egypt, industrial users account for the lion's share of the market, predominantly in power generation, fertilisers, cement, and steel manufacturing. Industrial and commercial customers, such as the manufacturing and tourism industries, are similarly the bulk of Taqa Gas' sales (97%)—higher-margin (60% gross margin) compared to residential customers (25% gross margin), which represent a more marginal 3% of the company's gas sales. On a blended basis, Taqa Gas generates a gross margin of 40%. Among the areas covered by Taqa Gas' Nile Valley Gas concession is Upper Egypt (from Beni Suef to Aswan and Toshka), where the basic infrastructure advantageously allows for quicker and lower-cost construction. The high population density in rural areas also means higher returns per km.

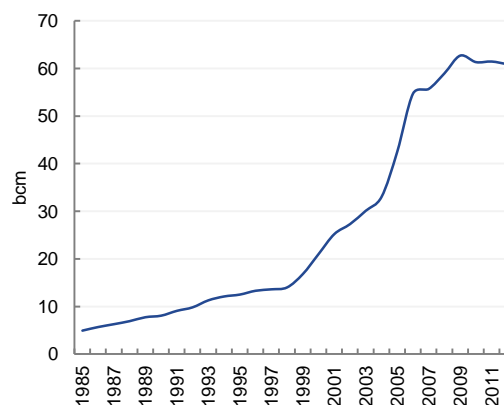
As of September 2014, Taqa Gas had provided gas connections, as well as operational and maintenance services to a total of 545k Egyptian households and 159 power, commercial, and industrial clients. The company's residential household portfolio represents 9.9% of the total 5.51mn household connections in Egypt, ranking it second to EKH's subsidiary Natenergy, which connects close to 900k households, implying a share of 16.3%, on our calculations.

Households connected to the national gas grid (mn)



Source: World Bank, CI Capital Research

Egypt's gas production (1985-2012)



Source: BP Statistical Review of World Energy (June 2013)

Taqa Gas' profit margins are unaffected by changes in natural gas prices, although higher prices are positive for the company, as they would help improve its cash conversion cycle, given it typically collects receivables on a monthly basis but pays the government quarterly. Taqa Gas charges EGP2.5k/connection: EGP1.5k from the client as upfront payment and another EGP1k collected from the state-owned gas holding company over a three-year period, to cover installation costs (construction, metering, and piping). A pre-determined fee is then set and collected with the monthly bill, irrespective of the price of gas. Taqa Gas's growth drivers would be any upward adjustments to the connection and/or collection fees, in addition to volume growth, as it would expand its household and industrial client base—but this would have to be a function of improved gas availability. Prior to 2013, gas availability was not a hindrance to growth, and Taqa Gas had been growing its gas sales at a compound annual rate of 9.6% from 2009-12. Going forward, the scope for volume growth remains substantial, as more than 70% of Egyptian households rely on butane gas cylinders, and each unconnected household costs the government an additional USD200 in subsidies every year, according to the World Bank.

Aside from a continued deterioration in gas availability going forward, the main downside risks for Taqa Gas would be higher-than-expected labour cost inflation or EGP devaluation, as 80% of the company's raw material costs are USD-based, which are difficult to pass-through due to the lack of cost-escalation clauses. In 2010, the company's gross margin stood at 50%, but this figure has now fallen to 40% due to labour cost inflation and EGP weakness, despite the increase in monthly residential admin collection fees from EGP1.75 to EGP4.0 per client. This remains attractive, with local peer Natenergy generating a 35% gross margin. Our gas distribution volume assumptions are also more prudent than the company's, to account for the risk of nationwide gas shortages.

Taqa EPC is an integrated utility service provider and a subcontractor for the group's Egyptian, Qatari, and UAE operations. As the company's construction arm, it successfully has and continues to work on the delivery of infrastructure for Taqa Gas' four concessions. The unit generates a 14% gross margin, representing 13% of Taqa Arabia's 2013 gross profit, the smallest share among the company's four different units.

Taqa Power (45% of Taqa Arabia 2013 gross profit): Taqa Power is a leading private sector developer with contracted generation, distribution, and an O&M capacity of c850 MW for commercial clients in Egypt. In our view, Taqa Power is well-positioned to capitalise on rising opportunities in Egypt's power market, in light of ongoing reform measures.

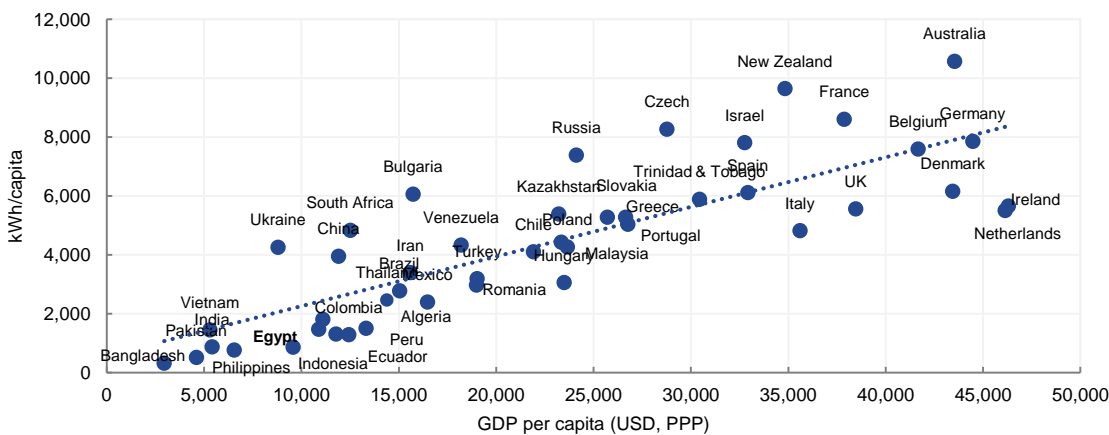
Although the residential sector consumes 40% of generated electricity, its share in Egypt's total electricity subsidy bill is at 70% and rising, as residential sector tariffs are not as high as commercial and industrial tariffs. The residential sector is also the main contributor to peak demand (45%), as its consumption pattern has lower elasticity. High increases in demand of 7% p.a. (and higher increases in peak demand of 11% p.a., led by the household sector) as power remains heavily subsidised means that substantial investments are now required. Except the fiscal budget is tight and fuel supply is limited. The government has begun addressing the fact that tariffs were less than the economic cost, raising electricity prices in July 2014, and more importantly announcing that this action comes as part of a medium-term plan to liberalise power prices in five years' time. The magnitude of the increase (15-66% depending on consumption bracket), along with other reform measures taken to date (outlined below) is unprecedented. As a result, we are bullish on the government's USD23bn power-project spending pipeline (2015-17), contingent on continued policy follow-through. This is equivalent to 3.7x the power projects currently underway and is separate from the private industrial sector's initiatives to ensure captive power supply in order to avoid disruptions. There is an estimated 32,000 MW of new capacity needed across the country by 2020. Taqa Power is bidding, as part of a consortium with Neoen, for a 200 MW solar project in Kom Ombo (20 MW x 10 areas), and was pre-qualified for it by EETC. Following this, Taqa and Neoen signed an agreement to extend their cooperation in the renewable energy sector.

Egyptian Electricity Holding Company (EEHC) owns c90% of generation, 100% of transmission, and c99% of distribution

	Current market	Potential
Generation: Public (90%)	<p>Public: 6 generation companies, 27GW production capacity</p> <p>Private: 3 20-year BOOT contracts for 2GW, with all output sold directly to Egyptian Electric Transmission Co EETC</p>	<p>Jul 2014 power price increases (by a blended 50% vs. historical average of 5% p.a.) and plan to liberalise power prices by 2019 should encourage both public and private generation investment.</p> <p>Self- and co-generation, feed-in-tariff, and the coal-usage approval should also spur investment in generation, as oil/gas availability had been a concern before</p> <p>Private generation companies will have the right to conclude direct bilateral contracts with clients</p>
Transmission: Public (100%)	<p>Public: EETC is the sole transmission entity, purchasing all output from generation plants</p>	<p>Establishment of Transmission System Operator to provide assurance of its independence and full unbundling from the rest of the power supply chain</p> <p>There are no plans to allow private sector participation in transmission</p>
Distribution: Public (99%)	<p>Public: 9 public companies, purchase power from EETC to 28mn customers</p> <p>Private: 15 private electricity distributors are licensed, with Taqa Arabia claiming it is the largest private player</p>	<p>Government is introducing reform to allow direct, bilateral agreements between private producers and end-users</p> <p>By introducing competition, those with better efficiency and services should fare better</p>

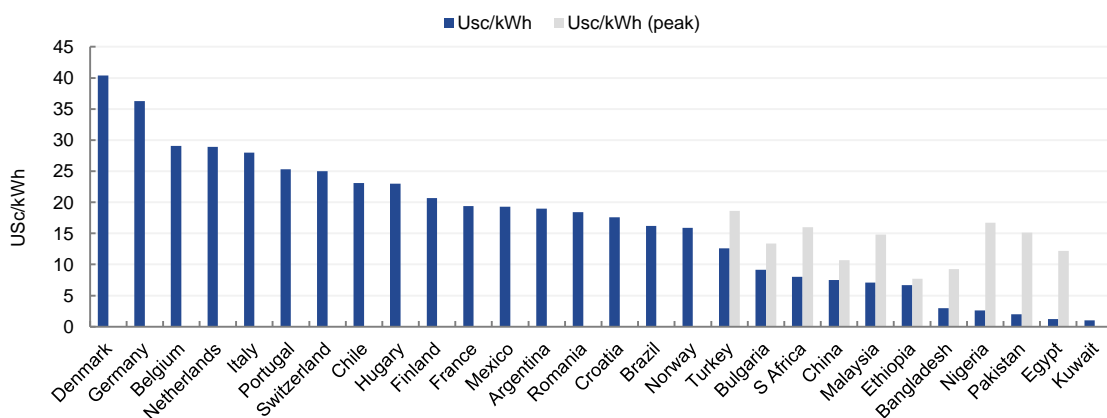
Source: Ministry of Electricity, CI Capital Research

Egypt on electricity generation per capita vs. GDP per capita



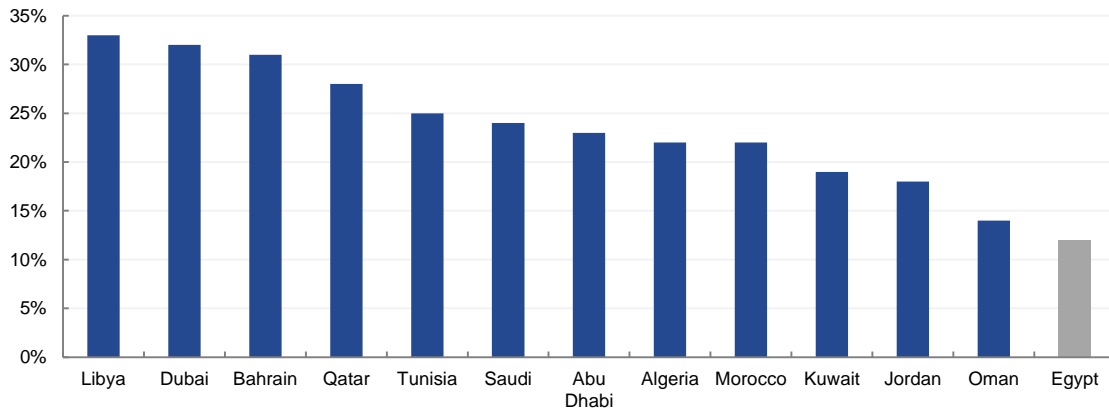
Source: BP Statistical Review, World Bank

Power remains very cheap in Egypt even after the Jul 2014 hikes



Source: Energy Information Administration (EIA)

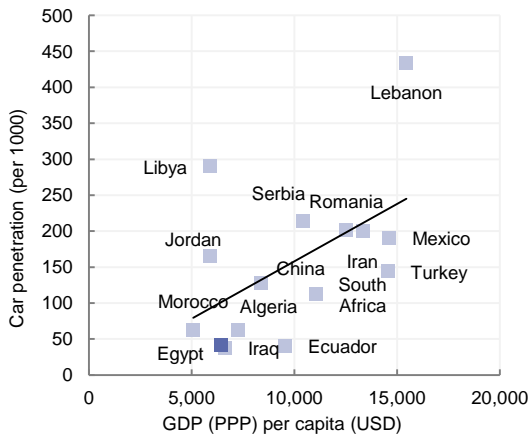
Egypt has the lowest reserve margins in MENA (2012)



Source: MEED Insight

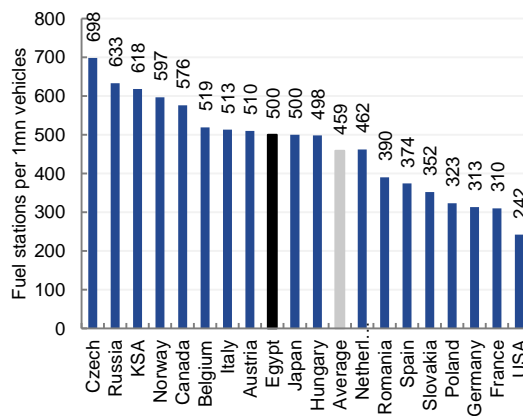
Taqa Fuel Marketing: Taqa also runs a relatively small but strategic oil marketing and fuel products distribution business, with 42 stations by the end of 2014 implying a market share of approximately 1.5%, and a target to grow its presence to 117 stations by 2019 (107 fuel stations and 10 gas stations). Taqa Marketing is selective on the location of its stations, which cost EGP3mn/station to rent or EGP6mn/station if owned. The company also has a storage unit in Suez, for fuel security reasons and working capital management, and plans to bring a second storage terminal on stream by 2017. The supply of fuel stations in Egypt is relatively abundant, standing at 500 stations per 1mn vehicles vs. a sample average of 459 stations per 1mn vehicles. That said, vehicle penetration in Egypt remains low; for PCs, vehicle penetration is 33% lower than markets with comparable income levels, suggesting that station traffic, or sales per station, should grow. The second driver to revenue growth for Taqa’s marketing unit should be reduction of fuel subsidies, as the government typically increases spreads for station operators when it raises the regulated fuel price, given that fuel purchasing costs typically represent 70-80% of CoGS.

PC penetration vs. GDP per capita PPP for EM (2011)



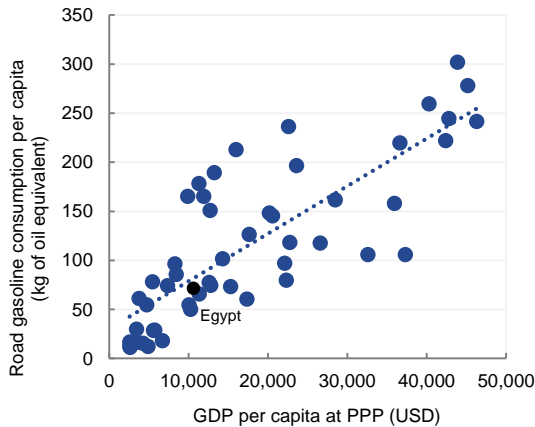
Source: World Bank, IMF, CI Capital estimates

Fuel stations per 1mn vehicles (2011)



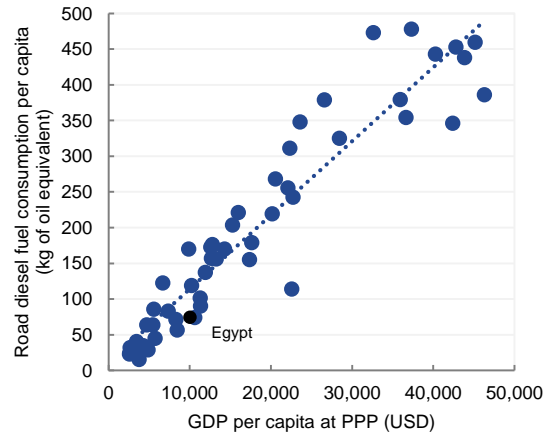
Source: CBRE European Petroleum Retail Sector MarketView, Organisation of Motor Vehicle Manufacturers (OICA), Aldrees, Taqa, CI Capital Research

Egypt on-road gasoline consumption per capita (2013)



Source: BP Statistical Review of World Energy (June 2013)

Egypt on-road diesel consumption per capita (2013)



Source: BP Statistical Review of World Energy (June 2013)

Taqa Arabia key operating assumptions

(EGPmn)	2013	2014e	2015e	2016e	2017e	2018e
Gas distribution						
Gas sales (bcm/y)	4.80	3.80	4.68	5.94	6.46	6.56
% y-o-y	(11.1)	(20.8)	23.2	26.9	8.8	1.5
Industrial customers	145	165	172	179	186	193
Additions	27	20	7	7	7	7
Residential customers	547,377	557,377	620,000	740,000	860,000	980,000
Additions	59,713	10,000	62,623	120,000	120,000	120,000
Revenue	182	144	175	219	234	234
Gross profit	73	58	70	87	94	94
Gross margin (%)	40.4	40.0	40.0	40.0	40.0	40.0
Construction						
Revenue	207	199	257	257	280	285
Gross profit	29	26	36	36	39	40
Gross margin (%)	13.9	12.8	14.0	14.0	14.0	14.0
Power generation & distribution						
Generation	134	133	145	143	375	375
Distribution (global)	356	480	544	582	622	666
Distribution (Taqa industrial zone)	169	235	298	434	486	539
Sold electricity (mn kw/hr)	658	848	987	1,158	1,483	1,580
% y-o-y	n/a	29	16	17	28	7
Regional						
Revenue	27	36	49	56	62	66
% y-o-y	0	0	35	15	11	6
Gross profit	7	9	12	14	16	17
Gross margin (%)	24	26	25	25	25	25
Fuel marketing						
Fuel stations	26.0	34.0	53.0	73.0	93.0	100.0
Gas stations	7.0	7.0	7.0	7.0	8.0	9.0
Terminals	1.0	1.0	1.0	1.0	2.0	2.0
Total no. of stations	34.0	42.0	61.0	81.0	103.0	111.0
Total fuel sales volume (000 t)	412	755	1,133	1,416	1,699	1,869
% y-o-y	0.0	83.1	50.0	25.0	20.0	10.0
Total lube oil volume (000 t)	1.8	5.5	5.5	7.2	8.6	11.0
Revenue	541	1,133	2,022	3,093	4,390	5,643
% y-o-y	10.3	109.3	78.6	52.9	41.9	28.6
Gross profit	14.4	36.2	64.7	99.0	140.5	180.6
Gross margin (%)	2.7	3.2	3.2	3.2	3.2	3.2
Taqa Arabia (group)						
Revenue	1,228	1,802	2,864	4,048	5,509	6,807
Gross profit	225	239	320	385	479	533
Gross margin (%)	18.4	13.3	11.2	9.5	8.7	7.8
G&A	111	126	129	134	154	157
EBITDA	136	158	263	352	463	547
EBITDA margin (%)	11.0	8.8	9.2	8.7	8.4	8.0

Source: QH, CI Capital estimates

Valuation

Summary of DCF valuation findings for Taqa Arabia

(EGPmn)	2014e	2015e	2016e	2017e	2018e	2019e
Operating profit @ 25% tax rate	86	146	191	248	288	317
Depreciation	43	69	97	132	163	193
Δ in WC	83	0	(70)	76	82	83
Capex	(87)	(223)	(237)	(112)	(112)	(68)
FCF	125	(8)	(18)	344	422	525
WACC (%)	13.1	13.1	13.1	13.1	13.1	13.1
Discount period	-	1.00	2.00	3.00	4.00	5.00
Discounted cash flow	125	(7)	(14)	238	258	284
PV of free cash flows	759					
Continuing value	5,367					
Discounted continuing value	2,903					
EV	3,661					
Add cash (Sep-14)	669					
Less debt (Sep-14)	311					
Equity value	4,019					
Equity value to QH (62.5%)	2,512					
Shares (mn)	1,600					
DCF value to QH (EGP)	1.57					

Source: CI Capital estimates

Egyptian Refining Company (ERC)

Project background

In order to address the growing imbalance in the supply and demand of refined oil products in Egypt, ERC was established in July 2007 to design, construct, and operate a new hydro-cracking/coking facility adjacent to the existing Cairo Oil Refinery Company (CORC), which was built in 1969. This location is ideal to supply the greater Cairo and Upper Egypt areas, which together comprise 65% and 44% of the country's total fuel oil and diesel consumption. ERC will utilise feedstock (straight-run atmospheric residue, a fuel oil) from the CORC facilities' existing units and will further process it to produce additional high-quality petroleum products essential to consumers in Cairo and Upper Egypt. This PPP will enable ERC to decrease Egypt's dependency on petroleum imports by c50% to c2.3mn tpa, when fully operational. QH owns 15.2% of the project, co-investors (including JIF) 33%, Qatar Petroleum International (a wholly-owned subsidiary of the state-owned Qatar Petroleum) 28%, and EGPC holds the remaining 23.8%.

ERC has signed a lump sum turnkey EPC contract worth USD2.2bn (including amendments as the execution date was delayed by six months due to a delay in the handover of the land from the government) with a consortium consisting of the South Korean GS Engineering (65%) and Japanese Mitsui (35%) for plant construction, which began in 2H13. Construction is now over 40% complete and the start date is planned for early 2017, with 2018 set to be the refinery's first 12 months of operation with an EBITDA target of USD700mn, given the closing prices of oil and fuel products in 2014. The total cost of the project, including financing expenses, is expected to stand at approximately USD3.7bn, of which USD2.35bn will be debt-funded. Once commissioned, EPROM (Egyptian Projects Operations and Maintenance Co.) will take over ERC's operation and maintenance, as it is owned and controlled by ERC's strategic state-backed shareholder EGPC.

A simple refiner, in an aged market, with an ideal location

ERC will be a coking/hydro-cracking complex, and while it is not subject to the negative margins generated by the hydro-skimming stage (as is the case with CORC), it remains a simple refiner with lower margins than complex refineries that can extract more from a heavy/sour barrel of oil, maximising yields. Simple and complex refineries will have different equipment. The US has more complex refineries than any other country, followed by China, and various European countries. Generally, the configuration of a complex refinery is geared towards making gasoline, which requires catalytic cracking, whereas a simple refinery focuses on middle distillate, which requires hydrocracking. That said, ERC has a lot to bring to Egypt's refining industry: i) it will add 13% to the country's refining capacity, ii) it will improve the industry's age which currently averages over 50 years, and iii) it will enjoy a strategic location adjacent to CORC, which means it will easily access crude oil, and also remain close to their main consumers in Cairo and Upper Egypt, which represent 65% and 44% of total fuel oil and diesel demand.

ERC vs. Egypt's oil refining industry: 9 refineries, 5 main locations

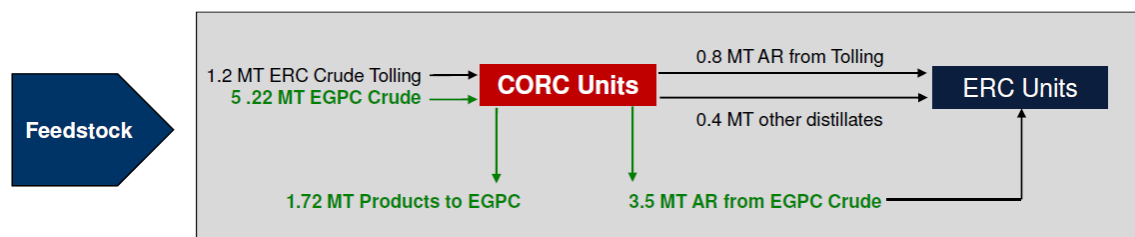
Refinery	Start-up	Location	Capacity (b/d)	% of total refining capacity
AMOC	2002	Alexandria	34,447	4
MIDOR	2001	Alexandria	100,000	13
Asyut	1987	Assiut	47,000	6
Tanta	1973	Tanta	35,000	5
Ameriya	1972	Alexandria	78,000	10
Cairo Oil (CORC)	1969	Cairo	160,000	21
Alexandria	1957	Alexandria	100,000	13
El Suez	1921	Suez	66,400	9
El Nasr	1913	Suez	146,300	19
Total			767,147	
ERC	2018	Cairo	97,489	13

Source: QH, CI Capital Research

Favourable refinery economics thanks to supply and product off-takes

ERC is designed to produce over 4mn tpa of refined products (diesel, jet fuel, naphtha, reformates, LPG, and fuel oil), including 2.3mn tpa of diesel that will be allocated to use in light passenger and commercial vehicles. The diesel produced will be in line with Euro V standards, a very-high quality fuel that follows European emission standards. The sale of ERC’s refined products to the state-owned EGPC (Egyptian General Petroleum Company) will be implemented through an offtake agreement on a ‘take or pay’ basis in USD, based on international product prices. The terms of the signed agreements with EGPC commit the state-owned company and its affiliates to a 25-year feedstock supply contract starting from ERC’s first day of commercial operations. To elaborate, the agreement stipulates that EGPC must i) supply and deliver a minimum of 3.5mn tpa of atmospheric residue to ERC, at Mediterranean high sulphur fuel oil (HSFO MED FOB PLATTS) prices plus a 4.4% premium, and ii) provide ERC with additional quantities of atmospheric residue on a priority basis.

Integration between the government (CORC) and ERC

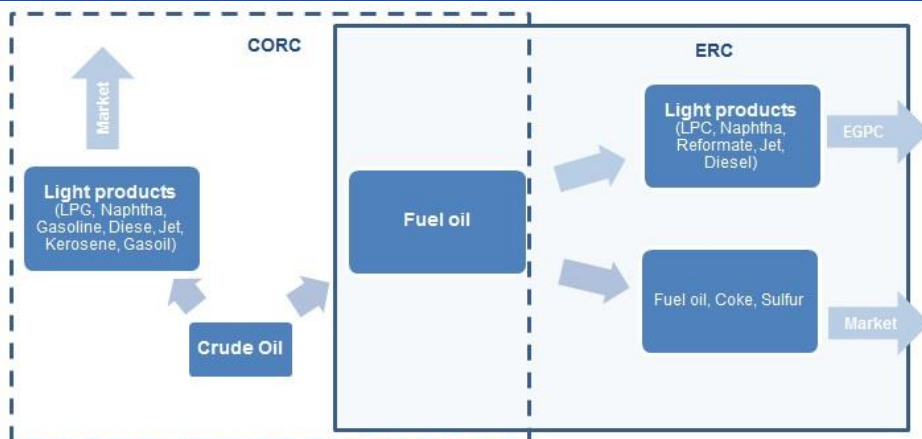


Source: QH

The government commitments are win-win given ERC offers a substitution to imports

With ERC producing approximately 3.5mn tpa of transportation fuels for Greater Cairo, the main consumption center, EGPC expects USD300mn in annual cost savings from avoided transportation and insurance costs, eliminated product shipment losses, as well as revenues generated from storage and processing fees. The specifications of fuel supplies will also improve compared to what is currently being consumed; ERC will produce European grade diesel (EU V) and IATA worldwide specification jet fuel, as well as eliminate 96k tpa of sulphur currently being released into the environment from burning atmospheric residue/fuel oil sold in the market. Over the next decade, Egypt is expected to experience a large surplus of heavy fuel oil and a growing deficit in middle distillates (diesel and jet fuel) and gasoline—products ERC is specialized at manufacturing utilizing residual heavy fuel oil from Egyptian refineries.

ERC will buy residual fuel oil from state-owned CORC for further refining into higher-value products, of which Egypt has a deficit



Source: QH

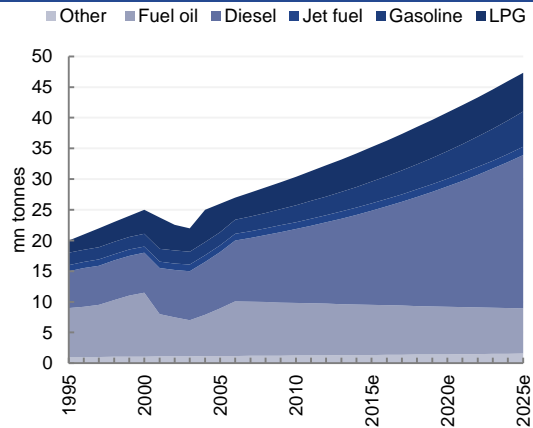
ERC's production capacity and end-buyer

Product	Ktpa ¹	Buyer
LPG	79	EGPC (88% of output)
Naphtha	336	
Reformate	522	
Jet fuel ²	599	
Diesel ³	2,255	
Fuel oil	315	
Subtotal	4,106	
Coke	453	Market (12% of output)
Sulphur	96	
Subtotal	549	
Total	4,655	

Source: QH.

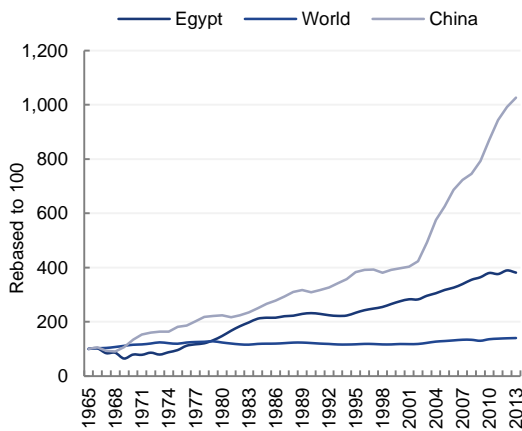
Note (1): Based on 350 days of operations a year. Note (2): IATA worldwide specification. Note (3): European-Grade (EU V)

Petroleum product demand in Egypt



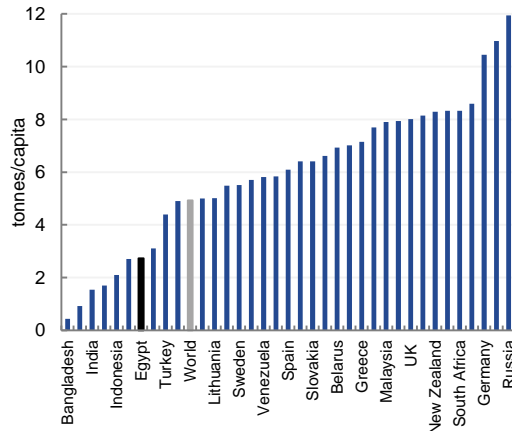
Source: QH

Egypt's CO2 emissions per capita is growing fast



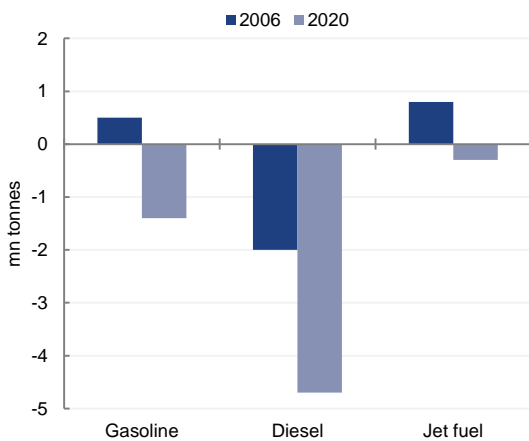
Source: BP Statistical Review (2013)

Egypt vs. other markets on CO2 emissions per capita



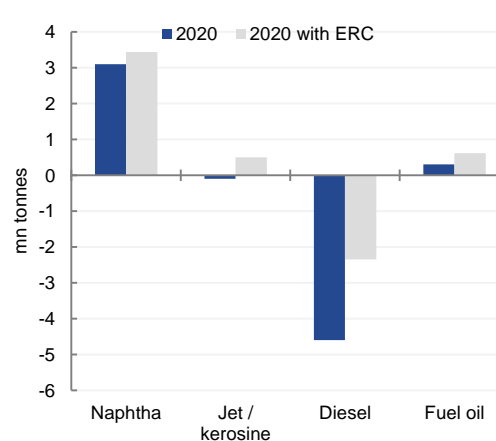
Source: BP Statistical Review (2013)

Egypt's forecast deficit in gasoline, diesel and jet fuel



Source: QH

ERC's output will reduce Egypt's import dependency, particularly for diesel



Source: QH

ERC margin forecasts and valuation

ERC's margins are a mix of regular oil refineries that process crude oil (1.2mn tpa of Arab medium crude through CORC at USD3/barrel) and the upgrade margin that ERC generates on the 3.5mn tpa of atmospheric residue. Such downstream operations, which refine oil into gasoline and other products, become more profitable as the oil they use gets cheaper, so the current backdrop, in our view, is an attractive one for this unit. This is because prices of refined products such as gasoline do not typically fall as quickly as crude prices do, improving refinery economics via higher spreads. In order to arrive at our product price forecasts, we run a ten year historical regression between oil prices and those of ERC's product portfolio.

Summary of key operating assumptions for ERC

	2017	2018	2019	2020	2021	2022	2023
Capacity (k tpa)							
LPG	79	79	79	79	79	79	79
Naphtha	336	336	336	336	336	336	336
Reformate	522	522	522	522	522	522	522
Jet	599	599	599	599	599	599	599
Diesel	2,255	2,255	2,255	2,255	2,255	2,255	2,255
Fuel Oil	315	315	315	315	315	315	315
Coke	453	453	453	453	453	453	453
Sulfur	96	96	96	96	96	96	96
Total	4,655	4,655	4,655	4,655	4,655	4,655	4,655
Operating rate (%)	70%	97%	97%	97%	97%	97%	97%
Production (k tpa)							
LPG	55	77	77	77	77	77	77
Naphtha	235	326	326	326	326	326	326
Reformate	365	506	506	506	506	506	506
Jet	419	581	581	581	581	581	581
Diesel	1,579	2,187	2,187	2,187	2,187	2,187	2,187
Fuel oil	221	306	306	306	306	306	306
Coke	317	439	439	439	439	439	439
Sulfur	67	93	93	93	93	93	93
Total	3,259	4,515	4,515	4,515	4,515	4,515	4,515
Prices (USD/t)							
LPG	607	645	683	722	760	760	760
Naphtha	661	701	742	782	823	823	823
Reformate	694	736	779	821	863	863	863
Jet	681	724	767	811	854	854	854
Diesel	668	708	749	790	831	831	831
Fuel oil	388	418	449	480	511	511	511
Coke	90	90	90	90	90	90	90
Sulfur	150	150	150	150	150	150	150
Revenue (USDmn)	1,906	2,803	2,964	3,126	3,288	3,288	3,288
Cost (USDmn)	1,387	2,068	2,213	2,359	2,504	2,504	2,504
Quantity of crude oil (k tpa)	840	1,164	1,164	1,164	1,164	1,164	1,164
Arabian Gulf crude cif (USD/bbl)	70	75	80	85	90	90	90
Cost of crude oil (USD/t)	511	546	581	616	651	651	651
Quantity of gas feedstock (k tpa)	175	243	243	243	243	243	243
Cost of gas (USD/t)	50	50	50	50	50	50	50
Quantity of fuel oil feedstock (k tpa)	2,450	3,395	3,395	3,395	3,395	3,395	3,395
Cost of fuel oil (USD/t)	388	418	449	480	511	511	511
Cash profit (USDmn)	518	735	751	767	783	783	783
Cash margin (%)	27	26	25	25	24	24	2
Cash profit (USD/t)	159	163	166	170	173	173	173
Cash profit (USD/bbl)	21.8	22.3	22.8	23.3	23.8	23.8	23.8

Source: CI Capital estimates, Bloomberg, IHS Chemicals

Based on the commodity prices above, and a 97% operating rate at the refinery, we look for cash profits of USD23.8/bbl over our forecast horizon, which, assuming an SG&A that is in line with company guidance (USD70-80mn pa), points to EBITDA margins of 25%, or EGP5.4-5.7bn. Given limited expectations for growth in capex spending after the completion of the refinery in 2017, our model indicates annual free cash flows of EGP4bn—which we discount at a moving cost of capital (rising to 14.5% in our terminal year) to account for QH's changing capital structure. This leaves us with a 12-month valuation of EGP7.4/share, or EGP1.13/share given QH's 15.2% stake in ERC.

DCF valuation summary for ERC

(EGPmn)	2014e	2015e	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e ¹
NOPAT	(29)	(50)	(65)	2,818	3,494	3,551	3,608	3,634	3,601	3,566	3,425
Depreciation	-	-	-	0	772	774	776	778	780	782	784
Adjusted COPAT	(29)	(50)	(65)	2,818	4,266	4,326	4,384	4,411	4,380	4,348	4,209
Capex and WC	(11,238)	(6,316)	(4,136)	(1,431)	(1,122)	(246)	(247)	(249)	(121)	(56)	(56)
Free cash flow (FCF)		(5,881)	(3,608)	1,108	2,320	2,770	2,572	2,358	2,179	1,962	1,137
PVOP ¹	13,585										
PVTV ²	824										
EV	14,409										
Cash (Sep 14)	182										
Debt (Sep 14)	3,535										
Net debt	3,353										
Investments	-										
Equity value	11,056										
No. of shares (mn)	1,600										
DCF (EGP)	6.91										
QH share (EGP)	1.05										

Source: CI Capital estimates

Note 1: our DCF horizon runs till the 25 year-concession life ends in 2042, which is our terminal year. Note 2: Assuming 3% perpetual growth rate

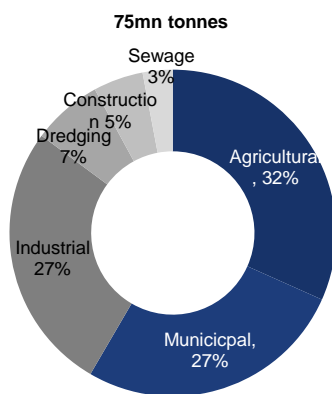
Project risks

Risks include construction delays, any changes to the company's feedstock supply and/or take-or-pay agreements with the government. Lower-than-expected terminal value is also a risk to our valuation, as the parties may agree to term renewal prior to the end of the 25-year contract. If in the unlikely event that there is no agreement, a valuation process is initiated to determine ERC's value. EGPC would then be contractually mandated to pay the sponsors for the asset, should negotiations move in that direction.

Tawazon

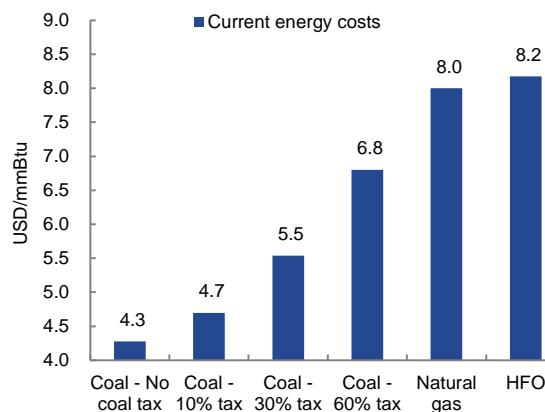
Tawazon, 47.9%-owned by QH, is the country's largest solid waste management firm. In addition to collecting and processing waste, Tawazon also is in the business of constructing sorting and composting facilities in Egypt, but it remains small in size, as the market is still in the very early stages of development; the majority of agricultural solid waste is either burnt or processed by the highly primitive informal players who currently dominate the market. It becomes increasingly difficult dealing with municipal waste as population figures swell (Cairo: 15mn, Alexandria: 5mn). In 2013, Tawazon collected 214k tonnes of waste, and has collected up to 522k tonnes in previous years, but this remains a very marginal 1.2% of the country's total agricultural and municipal waste. The unit represents 2% of QH's consolidated EBITDA in 9M14, before one-offs. Looking forward, we expect Egypt's ongoing energy bottlenecks, as well as the removal of energy subsidies, to instigate high levels of demand for waste as an alternative energy solution. Tawazon's unique presence as an organised player means it has the first mover advantage to capture this growth. The company converts agricultural and municipal waste, together c60% of the country's 75mn tonne waste market, into i) alternative fuels for industry and ii) other useful products, like compost and animal fodder.

Egypt's annual solid waste by source



Source: QH, EEAA

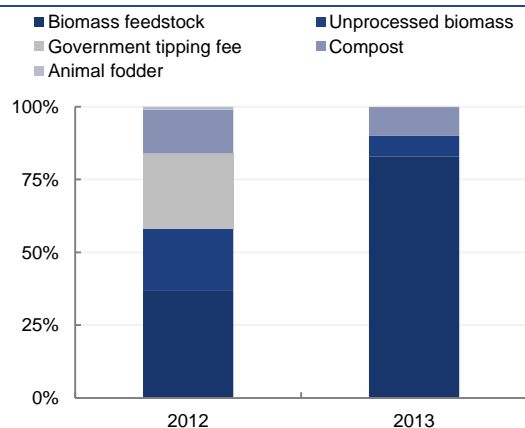
Current energy costs in cement manufacturing



Source: CI Capital Research

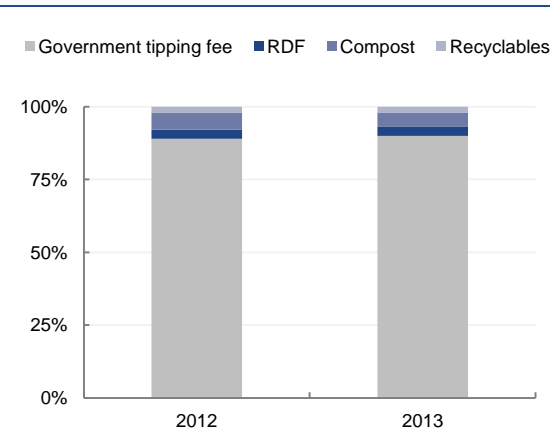
Tawazon has long term agreements with the government to receive, sort, treat, and landfill up to 547k tonnes of waste p.a. in the south of Cairo, and was recently awarded a similar contract for 1.1mn tpa in the governorate of Dahaklia. The company is trying to diversify away from such government generated revenues. Aside from product sales proceeds, tipping fees paid by the Egyptian Environmental Affairs Agency (EEAA) are a source of revenue. Non-payment from the government—as was the case in 2013—causes the company to reduce its waste collection efforts, the main reason behind the c59% y-o-y plunge in agricultural waste collection revenue in 2013. The company is still unclear as to the potential renewal of agricultural waste collection contracts and the new pricing structure. As per QH's release, outstanding receivables from the EEAA stand at EGP30mn.

Agricultural waste management revenue breakdown



Source: QH

Municipal waste management revenue breakdown



Source: QH

Other than the government, the main source of revenue growth for the company is the local cement industry, in our view. Cemex, Lafarge and Italcementi (together c43% of the country's cement manufacturing capacity) are all clients of Tawazon. While CI Capital calculates that c80% of the cement industry has plans to migrate to coal, the Ministry of Environmental Affairs has required these companies to use a specific amount of alternative fuel (estimated at c20% of respective energy needs), such as biomass, in their energy mix in an effort to limit the environmental damage resulting from coal usage. At the same time, because Tawazon is unique in such an underdeveloped market, it has strong pricing power and is able to sell its various alternative fuel products at prices that are linked to the prices of the energy sources that each cement plant is exposed to (fuel oil, natural gas, and coal). As such, it captures upside, as the subsidies of those fuels are removed. To illustrate the extent of the shortness in residue-derived fuel (RDF) supplies, Tawazon's calculations imply that collecting and processing the country's waste at the most efficient rate possible would still only suffice c30% of the country's total clinker production needs by 2017, and hence why the maximum substitution rate the Ministry of Environment is calling for is closer to 20%.

Industry energy migration – status quo by producer

Producer	Capacity (mn tpa)	Market share (%)	Current energy source	Migration status
Italcementi	12.0	17.8	State-supplied	Converting
Lafarge	10.6	15.7	60% state, 40% independent	Partially converted
Cemex	6.5	9.6	State-supplied	No announced plans
ACC	5.0	7.4	20% state, 80% independent	Partially converted
Titan	4.5	6.7	State-supplied	Converting
Cimpor	3.7	5.5	State-supplied	Converting
National Cement	3.5	5.2	State-supplied	Converting
Sinai Cement	3.2	4.7	State-supplied	Converting
El-Arish Cement	3.2	4.7	State-supplied	No announced plans
Misr Beni Suef	3.0	4.4	State-supplied	Converting
Misr Cement-Qena	2.0	3.0	State-supplied	Converting
Minya Cement	2.0	3.0	State-supplied	Converting
South Valley Cement	1.5	2.2	State-supplied	Converting
El Sewedy Cement	1.5	2.2	State-supplied	Converting
Wadi El Nile Cement	1.5	2.2	State-supplied	No announced plans
El Nahda Industries	1.5	2.2	State-supplied	No announced plans
BMIC	1.5	2.2	State-supplied	No announced plans
Medcom Aswan	0.8	1.1	State-supplied	No announced plans
Shoura (Spegyco) ¹	0.6	0.9	n/a	n/a
Total	68.1	100.0		

Source: Company announcements, CI Capital Research
Note (1): Shoura Cement is a cement grinding facility

Tawazon estimates that collecting and processing Egypt's municipal waste very efficiently would satisfy c40% of the country's clinker manufacturing needs in 2014, c30% of our 2017 clinker production estimates

	(%)	2014e	2017e
Calorific value need for Egypt's clinker production			
National clinker production (tonnes)		51,075,389	65,272,727
Conversion from Kcal to mmBtu		3.6	3.6
Total need for Egypt's clinker production (mmBtu p.a.)		182,412,103	233,116,883
Maximum country-wide RDF fluff production			
MSW produced (tonnes p.a.)		20,000,000	20,000,000
Organic material	49		
Reject	50		
Others	1		
Reject to RDF fluff (production conversion rate in tonnes)	40	4,000,000	4,000,000
RDF fluff calorific value (mmBtu per tonne)		18.0	18.0
Total RDF fluff production (mmBtu)		72,000,000	72,000,000
Maximum substitution rate (%)		39.5	30.9

Source: Tawazon, Ministry of Industry and Trade, CI Capital estimates

Mashreq

Mashreq (54.9%-owned) signed a 30-year concession agreement with the state-owned East Port Said Port Authority to build Egypt's first independent tank terminal to provide liquid bulk petroleum products storage for the Middle East and Mediterranean markets. The terminal would also offer bunkering and blending services for ships transiting the Suez Canal, as it will be constructed on a 210k sqm land plot located close to the strategic Suez Canal entrance, giving it access to heavy traffic to the extent that the company expects 14x annual turnover of its tanks capacity. The 25-year concession was drafted on a BOT, and is extendable by one year for every five years that the project achieves at least 90% of its throughput targets.

QH is currently involved in non-exclusive negotiations regarding potential partnerships to build and operate the storage and bunkering terminal. As part of the concession agreement, Mashreq has a three-year grace period for construction that expires in May 2017, so we would expect it to select its two partners (one for bunkering and another for storage) by mid-next year, since its 18-month construction lead-time means completion before the May-2017 deadline; our understanding is that the licenses (one for bunkering and another for storage) would otherwise lapse. There are multiple partners within the bunkering industry, such as Vittol, but selecting a partner for storage activity may prove more of a lengthy process. While QH expects to generate sustainable revenue of USD135mn and EBITDA of USD80mn from Mashreq, we choose to value the project at book, primarily to reflect the historical cost of land, until the two partners are selected and construction begins.

Cement [c40% of SoTP valuation]

- QH's cement exposure is now centric to Egypt (and North Sudan, to a much lesser extent), with Algerian cement assets up for sale and political instability in Iraq and Syria reversing investment plans
- We are very bullish on the Egyptian cement sector; we see the government's infrastructure drive alongside housing demand driving cement consumption up 8% in each 2015 and 2016 vs. 1.8% in 2014
- QH's Egyptian plant has deployed capex to convert to coal by May 2015, reducing energy costs by 15%—assuming a 30% tax on landed coal costs is put into effect

ASEC Holding

QH's cement unit, ASEC Cement, used to have a more regional focus, with greenfield plants in Algeria, Iraq, Syria, and North Sudan. But, the operating backdrop turned against the company in each of those markets, except Egypt. QH discontinued its investments in Iraq and Syria, while the two Algerian units, Zahana and Djelfa, were reclassified as assets held for sale in 2Q14. The North Sudanese plant (1.6mn tpa) remains operational, and its capacity utilisation rate has recently improved from c40% to c90%, thanks to better natural gas supplies. We are particularly bullish on the company's Egyptian cement unit—a 2mn tpa plant in the south with a 3% local market share, which has plans to raise its capacity to 3.5mn tpa by 2017. In aggregate, the company's operational cement capacity is 5.6mn tpa, or 2.4mn tpa proportionate to its ownership, with another 6.1mn tpa (3.4mn to tpa on a proportionate basis) up for sale in Algeria. Aside from the company's cement holdings, ASEC Holding also owns a ready mix business, a cement plant engineering arm, and technical management services company that mainly operate in Egypt. The construction and technical management firms were loss-making through to 9M 2014 (-EGP10mn at the EBITDA level), but thanks to a recent jump in the construction backlog by EGP1bn and the extension of new awards for coal conversion projects and brownfield plants, we expect the units to generate EGP180mn in EBITDA by 2016.

QH's cement footprint

Plant	Market	Project	QH ownership (%)	Capacity (mn tpa)	Proportionate capacity (mn tpa)
Minya	Egypt	Greenfield, operational since Aug-13	51.0	2.0	1.0
Misr Qena	Egypt	Acquisition, 2 BoD seats. Operational.	27.6	2.0	0.6
Al Takamul	N. Sudan	Greenfield, operational since Oct-10	51.0	1.6	0.8
Zahana	Algeria	Acquisition, controlling. Operational.	35.0	2.8	1.0
Djelfa	Algeria	Greenfield (construction halted)	72.6	3.3	2.4
ASEC Syria	Syria	License. Project on hold.	n/a	1.7	n/a
Total				13.4	5.8
Total operational (Egypt + N. Sudan)				5.6	2.4
Total up for sale				6.1	3.4

Source: QH

Egyptian cement industry outlook

Reasons to be bullish on demand

Although in Jan-Nov 2014 local cement consumption was up 2.3% y-o-y to 46.6mn tonnes, consumption on a per capita basis stood at 591.2kgs—a five-year low—6% below the pre-revolution peak of 628.4kgs. Pent-up demand, the country resuming political transition, economic reforms, and the return of FDIs leave us bullish on both private and public sector construction demand, with our industry model suggesting that demand for cement will increase at an 8% CAGR over 2015-18e to 71.8mn tonnes. Construction demand in Egypt stood at 4.7% of GDP in 2014e, showing a growth of 3.4% y-o-y, driven by private demand, which in Egypt constitutes as much as 90% of total construction activity. While we remain bullish on private demand drivers, we expect to see comparatively higher growth in public activity as progress on recently awarded mega-projects kick-starts.

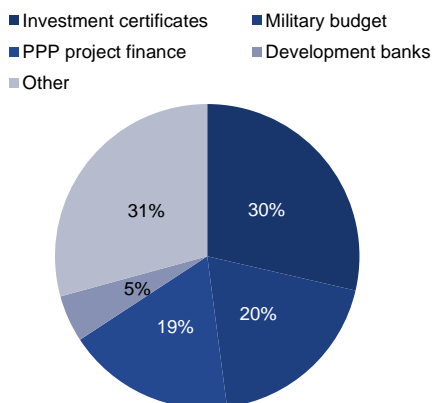
To illustrate, our database of major projects scheduled for execution in 2015 (those with a budget equal to or in excess of USD250mn) shows that the government issued USD20.5bn's worth of projects in 2H14—mainly in 4Q—with a further USD8bn due for award soon. In the past, the market was sceptical about such large-scale project activity materialising because funding was always a hurdle for the government. However, that 70% of these projects have secured funding, on our calculations: 50% from the military, 30% from Suez Canal investment certificates, and 20% from by PPP/BOOT project financing. We note that we exclude state projects, which we believe could be subject to delays, the largest of which includes the 1mn housing unit scheme (EPC value USD7.1bn), the Alex-Aswan high-speed rail (EPC value USD6.9bn), El Dabaa nuclear power plant (EPC value USD4.1bn), in addition to development work of the Suez Canal hub (EPC value USD2.7bn). The return of projects that had been held due to instability over 2011-13 could also instigate demand. While we expect the industry to become demand-driven, we acknowledge that construction site mobilisation and preparation works means cement consumption is likely to grow at higher rates from 2H15 onward. Also, parliamentary elections in 1Q15 could deter private construction demand, leading us to expect greater rises in pricing in the medium-term rather than in the nearer term.

Major public sector projects progressing

Public client	Project	Status	Sector	Award	Budget (USDmn)	EPC (USDmn)
Suez Canal Authority	New Suez Canal : 7 Tunnels	Execution	Transport	Aug-14	4,000	2,700
UEEPC	South Helwan power plant	Execution	Power	Sep-14	500	338
Suez Canal Authority	Suez Canal dredging: 1-6	Execution	Infrastructure	Oct-14	4,600	3,105
NAT	Cairo Metro network : Line 3	Execution	Transport	Nov-14	2,640	1,782
Min of Electricity	IPIC / OCI - Coal power plant	Study	Power	Dec-14	3,000	2,250
Military	Phase-III of emergency power	Bid	Power	n/a	2,300	1,553
Military	3.2k km roads	Execution	Transport	n/a	3,500	2,363
NREA	120 MW Wind Gulf of Zayt	Bid	Power	Dec-14	250	169
Min of Electricity	Gabal El Zeit Wind Phase II	Bid	Power	Dec-14	500	250
UEEPC	Abu Rawash expansion	Bid	Water	Jan-15	752	508
UEEPC	South Helwan plant	Bid	Power	Jan-15	200	135
National Railways	Railway restructuring - 1.2-1.3	Bid	Transport	Jan-15	550	371
NAT	Cairo Metro: Line 3 - phase III	Bid	Transport	Feb-15	1,200	810
EDEPC	El Shabab plant conversion	Bid	Power	Mar-15	900	608
EEHC	Dairut IPP	Bid	Power	Jul-15	2,500	2,000
NREA	Gulf of Suez Wind (250 MW)	Bid	Power	Oct-15	660	580
Egyptian Airports Co.	Sharm Airport: Terminal III	Bid	Transport	Dec-15	500	350
Total					28,552	19,870

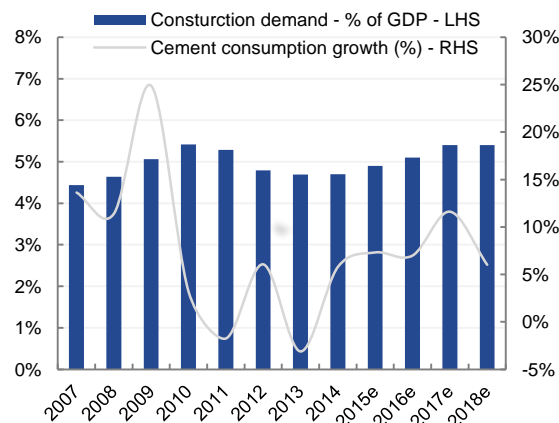
Source: MEED Projects, Ministry of Investment, PPP Central Unit

70% of projects have secured funding—19% off-balance sheet



Source: CI Capital Research

Construction (% of GDP) & cement demand growth (% y-o-y)



Source: Ministry of Planning, CBE, CI Capital estimates

Construction and cement demand assumptions

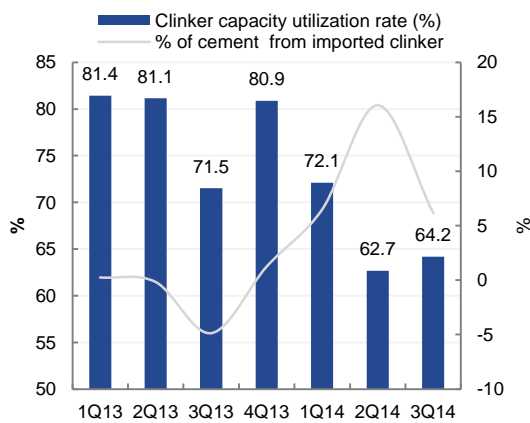
	2008	2009	2010	2011	2012	2013	2014	2015e	2016e	2017e
Construction demand growth (%)	10.8	14.2	12.9	(2.9)	3.2 ¹	1.5 ¹	3.4	8.2	8.7	11.5
Cement demand growth (%)	11.4	24.9	3.2	(1.7)	6.1	(3.1)	3.0	8.4	8.8	11.6
Local cement consumption (mn tonnes)	38	48	48	48	51	50	51	56	61	68
Per-capita cement consumption (tonnes)	510	623	628	604	628	598	599	635	676	738

Source: Ministry of Industry and Trade, CBE, Ministry of Planning, CI Capital estimates. Note (1): Estimated

Migration to coal means higher production as of 2015, but industry costs will not fall until 2017, except for early movers

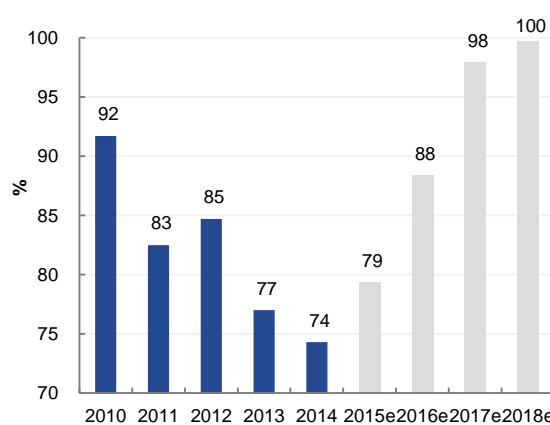
Clinker capacity utilisation rates stood at 71% in November 2014—a sharp deterioration from pre-revolution levels of 97%, as fuel from the government to the industrial sector remains in low supply. Some plants are worse off than others (fuel availability varies significantly by region and fuel type), so producers such as National Cement reported clinker operating rates of 37% for 9M14, while others reported higher rates of more than 95%. Minya Cement operated both its clinker and cement capacities at Jan-Nov 2014 averages of 92%. Generally, south-based producers that utilise heavy fuel oil are better off than those located in the north and rely on natural gas. While there are a handful of plants who are in a position to rely on coal in 2015, for the rest, costs will not fall until 2017—another factor backing our positive short-term pricing outlook. At the industry level, we believe industry operating rates will gradually rebound to 100% in 2018e as cement producers fully migrate. Our industry model suggests that demand growth will absorb incremental supply as producers improve capacity utilisation. In fact, next year we expect a marginal deficit, and predict that 0.9mn tonnes of cement will need to be imported.

Low energy availability led producers to import clinker



Source: Ministry of Trade and Industry, CI Capital estimates

Expect industry operating rates to improve as migration away from state-supplied fuel materialises



Source: Ministry of Trade and Industry, CI Capital estimates

Aside from rebounding operating rates, coal and alternative fuels are much cheaper than state-supplied fuels. The government is yet to issue the legislation for coal usage, but we believe this will include a tax rate of 30% on landed coal costs (EGP23/t), if not less, in order to encourage players to make the necessary investments, and also encourage investments in the sector, especially with us expecting the Egyptian cement market to become nearly self-sufficient in 2018e, with the potential risk of cement shortages if production declines. At a 30% tax rate, producers operating on coal and alternative fuels (70:30 mix) would enjoy diminished energy costs of USD5.5/mmBtu (EGP102/t), approximately 30% less than current average costs of USD8/mmBtu (EGP148/t) for state-supplied fuel. This means total cash costs should be 11% lower, all else constant.

Evolution of Egyptian cement industry costs and profitability

(EGP/t)	2014	2015e	2016e	2017e	2018e
Operating rate (%)	74.3	79.3	88.4	97.9	99.7
Retail selling price	675	707	744	810	830
Netback	630	657	688	747	762
Cash cost	403	421	452	374	396
EBITDA	227	236	237	373.2	366
EBITDA margin (%)	36.1	35.9	34.4	50.0	48.0

Source: CI Capital estimates.

Note (1): Cash costs do not account for clinker importing costs or premium for parallel market HFO supply.

Note (2): Cash costs are weighted by the estimated average cement production of cement producers

Egyptian cement industry supply/demand model

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015e	2016e	2017e	2018e
Supply													
Capacity (mn t)	39.8	41.8	43.3	46.5	52.7	59.1	62.4	66.6	67.4	69.2	70.8	73.9	73.9
Capacity utilization (%)	90.9	92.5	91.7	101.0	91.7	82.5	84.7	77.0	74.3	78.6	87.7	97.2	99.0
Total production (mn t)	36.2	38.6	39.7	46.9	48.3	48.7	52.9	51.3	50.1	54.3	62.0	71.8	73.1
y-o-y growth (%)	6.9	2.8	18.1	0.0	0.0	0.1	(0.0)	(2.4)	8.5	14.2	15.7	1.9	1.9
Exports (mn t)	5.85	4.21	1.34	0.28	0.02	0.69	2.02	0.24	-	-	1.37	4.08	1.35
% of production	16.2	10.9	3.4	0.6	-	1.4	3.8	0.5	-	-	2.2	5.7	1.8
Demand													
Domestic sales (mn t)	30.3	34.4	38.4	46.8	47.8	48.1	51.5	49.9	50.7	55.8	60.7	67.7	71.8
y-o-y growth (%)	-	13.6	11.4	22.1	2.1	0.6	7.0	(3.0)	1.6	8.4	8.8	11.6	6.0
Imports (mn t)	-	-	-	1.1	1.6	0.5	0.0	-	0.1	0.9	-	-	-
% of consumption	-	-	-	2.3	3.3	1.0	0.1	-	0.2	1.7	-	-	-
Total consumption (mn t)	30.3	34.4	38.4	47.9	49.5	48.6	51.5	49.9	50.8	56.7	60.7	67.7	71.8
y-o-y growth (%)	7.9	13.6	11.4	24.9	3.2	(1.7)	6.1	(3.1)	1.8	9.4	7.0	11.6	6.0
Population (mn)	71.3	73.6	75.2	76.9	78.7	80.4	82.0	83.6	85.8	87.8	89.8	91.8	93.9
Per-capita consumption (kgs)	425.1	468.0	510.3	623.2	628.4	604.3	628.5	597.6	591.2	635.1	675.7	737.5	764.6
y-o-y growth (%)	-	10.0	9.0	22.0	1.0	(4.0)	4.0	(4.9)	1.1	6.0	6.0	9.0	4.0
Net trade													
Net exports / (imports) (mn t)	5.9	4.2	1.3	(0.8)	(1.6)	0.2	2.0	0.2	(0.1)	(0.9)	1.8	4.6	1.8
Prices													
Selling prices - domestic (ex-factory, EGP/t)	331	362	440	511	450	380	420	550	675	707	744	810	830
y-o-y growth (%)	10.0	9.0	22.0	16.0	(12.0)	(15.6)	10.5	31.0	22.7	4.7	5.2	8.8	2.5
Selling prices - export (FoB, USD/t)	n/a	n/a	n/a	80.0	54.0	45.0	59.0	65.0	n/a	n/a	n/a	n/a	n/a
Cement demand vs. GDP demand													
Domestic cement demand growth	-	13.6	11.4	22.1	2.1	0.6	7.0	(3.0)	3.0	8.4	8.8	11.6	6.0
GDP growth	-	7.1	7.2	4.7	5.1	1.8	2.2	2.1	3.3	3.8	4.4	5.3	6.0
Cement demand multiplier	-	1.9	1.6	4.7	0.4	0.3	3.2	(1.4)	0.9	2.2	2.0	2.2	1.0

Source: Ministry of Industry and Trade, Ministry of planning, CAPMAS, CI Capital estimates

Minya Cement, QH's main cement asset

Altogether, we expect ASEC Holding, QH's cement arm, to generate EGP832mn in EBITDA in 2015, rising to EGP1.6bn by 2018e once Egyptian and North Sudanese plants have switched to coal, reducing energy costs alone by 25% for the company's Egyptian plant and by a more notable 60% for the company's North Sudanese plant which currently pays the state SDG4k/t for its fuel, while petcoke would cost SDG1.6k/t. Two other drivers are our positive Egyptian cement price outlook and Minya Cement's brownfield expansion plan, from the current 2mn tpa to 3.47mn tpa by the end of 2017. We like Minya Cement for a number of reasons:

Premium pricing. Our analysis shows that Minya Cement boasts pricing at a premium to the industry average and we attribute this to i) the plant's location, c240km south of Cairo, serving a relatively underdeveloped region and ii) the fact that c30% of the company's production is sulfate-resistant cement (SRC) which enjoys a an estimated EGP25/t EBITDA advantage over ordinary portland cement (OPC), which is traditionally sold by industry counterparts.

Energy diversification plans should ensure optimal operating rates. As a result of Egypt's energy policy changes, Minya Cement, like sector counterparts, is investing to diversify its energy sources, with a target to utilise coal for 70% of annual energy needs and RDF (residue derived fuel) for 30%, at an aggregate cost of less than EGP200mn, or USD14/t, to be completed by mid-2015. We estimate that this should reduce the plant's blended energy cost from USD8/mmBtu to cUSD7/mmBtu assuming a 30% coal tax, although this remains undecided as yet by the government. There are local market concerns over the availability of RDF in Egypt since the market is still young, but Minya Cement should have a secure supply of its RDF from Tawazon, which QH owns 47.9% of.

Cost savings from grid connectivity and waste-heat recovery (WHR) project. The company is not connected to the national electricity grid, and relies on diesel-fired generators for 100% of its power requirements. QH expects Minya Cement to connect to the power grid by end-2015, and in the meantime, capacity utilisation is unlikely to exceed 80%, as diesel is in scarce supply. Separate to its application for grid connectivity, QH is undertaking a WHR project for cUSD20mn, which will provide 8 MW of their 25 MW of annual power needs. Declining fuel availability, rising fuel costs, foreign currency shortages, increasing concerns about power reliability, and rising prices are strong drivers of WHR in the Egyptian cement industry. No-waste heat recovery power generation systems exist in the Egyptian cement industry, and Minya Cement is the first to make use of them. We expect unit power costs to drop by one-third starting January 2017, and as a result save the company cEGP14/t, equivalent to an estimated 2% of current netbacks.

Minya Cement would be the first to move toward WHR, although the case for WHR is high in Egypt

Country	Current WHR (MW)	WHR potential (MHW)	Concerns over power reliability	Industrial power prices (USD/MWh)	Sustainability of regulatory drivers
Brazil	None	190 - 340	No	120 - 170	Yes
Egypt	None	175 - 300	Yes	65 - 90	No
India	> 200	500 - 900	Yes	80	Yes
Mexico	None	170 - 300	No	117	No
Nigeria	None	70 - 130	Yes	50 - 100	No
Pakistan	> 100	50 - 100	Yes	130 - 170	No
Philippines	> 18	60 - 110	Yes	80 - 145	No
South Africa	None	55 - 100	Yes	80 - 150	Yes
Thailand	> 172	30 - 60	No	50 - 100	No
Turkey	> 80	150 - 280	Yes	100 - 150	No
Vietnam	> 11	165 - 310	No	60 - 70	No

Source: IFC, Jun-14

Summary of QH cement unit operating assumptions (Egypt and North Sudan assets)

(EGPmn)	2014e	2015e	2016e	2017e	2018e	2019e
Capacity (mn tpa) ¹	3,590	3,590	5,090	5,090	5,090	5,090
Production (mn tpa) ¹	2,365	3,177	3,339	3,712	4,683	4,758
Capacity utilisation rate (%)	65.9	88.5	65.6	72.9	92.0	93.5
Revenue	2,644	3,355	3,616	4,028	4,794	4,982
CoGS	1,821	2,219	2,355	2,485	2,889	2,883
Depreciation	165	188	203	224	236	237
Gross profit	657	949	1,058	1,319	1,669	1,862
Gross margin (%)	25	28	29	33	35	37
Other costs	63	81	87	97	115	120
Admin expenses	281	305	328	333	353	353
% of sales	13.0	11.5	11.5	10.7	9.8	9.5
EBIT	376	644	730	986	1,316	1,509
EBIT margin (%)	14.2	19.2	20.2	24.5	27.4	30.3
EBITDA	541	832	933	1,210	1,552	1,746
EBITDA margin (%)	20.5	24.8	25.8	30.0	32.4	35.0

Source: CI Capital estimates. Note (1): Excludes 27.55% equity stake in Misr Cement-Qena as equity accounted.

Summary of ASEC Holding DCF valuation findings

(EGPmn)	2015e	2016e	2017e	2018e	2019e	2020e
Operating profit @ 25% tax rate	451	511	739	987	1,132	1,127
Depreciation	188	203	224	236	237	235
Δ in WC and capex	(758)	(1,128)	(304)	(246)	(190)	(172)
FCF	(119)	(414)	660	976	1,178	1,190
WACC (%)	10.0	10.1	10.7	11.1	11.5	11.8
Discount period	1.00	2.00	3.00	4.00	5.00	6.00
Discounted cash flow	(108)	(342)	487	642	685	609
PV of FCF (2015-23e)	3,335					
PV of terminal @ 3% growth	4,158					
Enterprise value	7,492					
Add cash (Sep-14)	140					
Less debt (Sep-14)	3,487					
Equity value	4,145					
Shares (mn)	1,600					
DCF value (EGP)	2.59					
DCF to QH (EGP)	1.79					

Source: CI Capital estimates

Transport [7% of SoTP valuation]

- Monopolises cargo rail transport in Kenya and Uganda; targets raising rail traffic up to 12% from 7%
- The company's African rail operation should be neutral to the oil price decline, because while volume growth may slow, lower diesel prices should reduce fuel costs (c50% of total costs)
- In Egypt, river cargo demand would have to grow at substantially high rates given the low base: with river representing a minimal c0.5% of total cargo transported across the country

Africa Railways

Africa Railways (AR) was established by the state of Kenya and Uganda in 1948, and was privatised in 2006. AR's (28.2%-owned by QH) primary investment is a controlling 62.5% stake in Rift Valley Railways (RVR), which enjoys a 25-year concession to operate 2,352km of track connecting the Indian Ocean port of Mombasa, Kenya to the centers of both Kenya and Uganda. RVR is the single railway operator for both countries, having a monopoly in narrow-gauge railway (low-speed). It manages the mainline freight and passenger services between Mombasa, Kampala, and several other branch lines. Cargo transportation represents the bulk (c99%) of RVR's operations while passenger transport constitutes less than 1%. By 2020, AR expects to be the leading transport and logistics solution provider in Africa, with a strategic aim to i) improve the efficiency of the African railway sector, ii) increase the market share of rail traffic from 7% to 12%, and iii) improve the competitiveness of the northern corridor, a major transport route in East and Central Africa.

AR targeted rail line

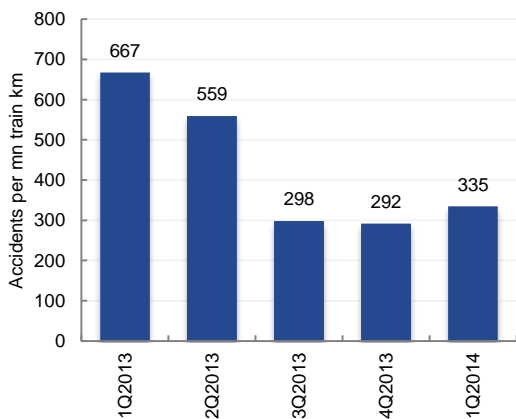


Source: QH

In 2011, AR formulated a 7-year strategic turnaround plan, which entailed a USD287mn capex program dedicated to accelerating the pace at which RVR will restore its infrastructure, putting the company on track to reach its long-term target of meeting market demand. The plan encompasses repairing a number of non-operational and damaged locomotives and wagons, replacing culverts in certain areas, and implementing IT systems.

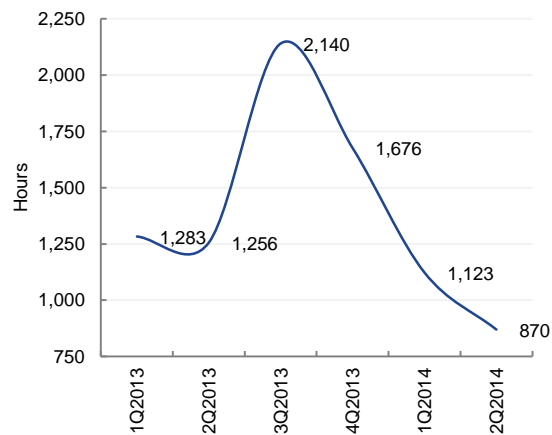
RVR is currently operating at 100%, and plans to bring 30 new locomotives on stream by June 2015, thereby doubling the company's handling capacity. RVR currently owns 32 locomotives, and its capacity is basically measured by the number of assets owned, adjusted by speed. AR is currently two years into the seven-year plan, which thus far has resulted in some margin improvement on the back of i) enhanced fleet fuel efficiency, ii) rationalised capacity, and iii) better management of fixed costs. Moreover, the upgrade has significantly improved the reliability and efficiency of the railway, now operating larger-capacity trains and, as a result, has seen improved loading capacity and reduced travel hours, in addition to a noticeable improvement in the total blockage time experienced (-32%) and accidents per mn-train kilometer (-51%). Just two years into the plan, FY13 revenues grew 5.1% y-o-y to USD71mn, and while EBITDA remained negative, it improved to—USD3.9mn from—USD9.9mn in FY12. The market size of Africa's railway transport has the potential to expand at a 10% CAGR during 2015-2030, and by the end of the program (2019), we expect the company to be generating USD123mn in annual EBITDA.

Average accidents per million train km



Source: QH

Total blockage time

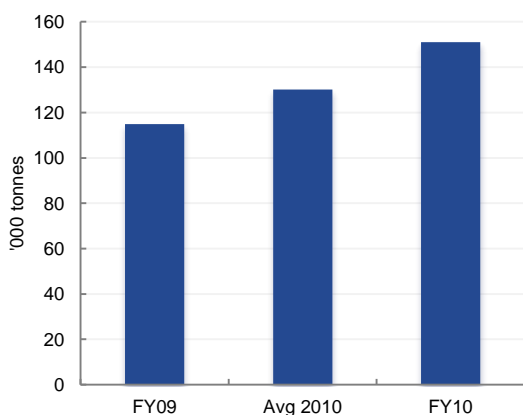


Source: QH

Industry overview and outlook

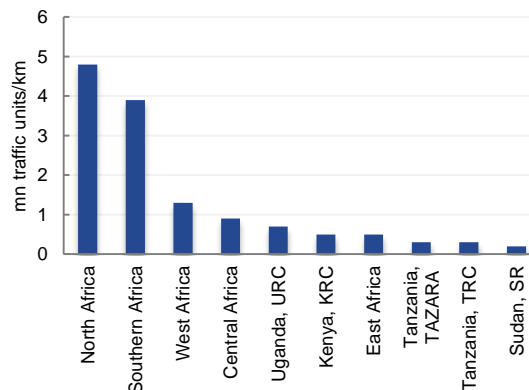
Although the Kenyan and Ugandan railway systems continue to lack innovation, proper maintenance, and updated infrastructure, transportation in East Africa as a whole has significantly evolved over the past years in terms of infrastructure and railway systems. These improvements happened on the back increased trading volumes and a steady expansion of its economies. As indicated by the East African Railways report, the ratio of transport growth to GDP growth has ranged between 1.0-1.5x, which leads to our expectation of 7.5-9.0% growth p.a. in transport, based on IMF forecasts of 5-6% GDP growth for Kenya and Uganda over our forecast horizon. Rail, which currently represents only 7% of overall transportation in these countries, should benefit disproportionately, we expect, given simultaneous capacity expansions and refurbishing/revamping works.

AR volume



Source: QH

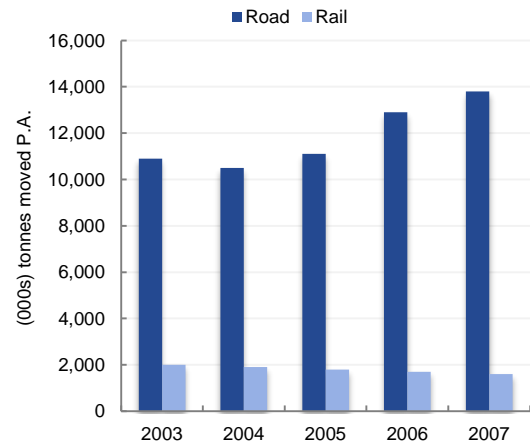
Million traffic units per route km



Source: Bullock 2009

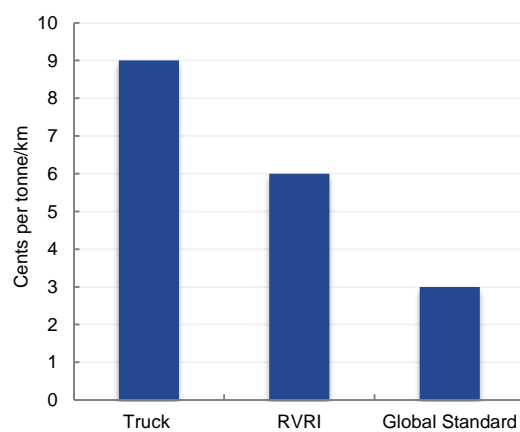
It is worth noting that rail transport currently faces a huge supply/demand gap, given RVR's capacity is stretched and that it is the sole operator in both countries. As it stands, the only competition comes from trucks, which are a significantly more expensive alternative route for moving goods. To put this into perspective, the cost to move 1 tonne by truck is USD0.9/km vs. only USD0.6/km via rail, which can be largely explained by the fact that rails consume half the quantity of fuel as compared to trucks.

Tonnes hauled by road vs. rail in East Africa



Source: QH

Trucking prices per t/km vs. RVR and global standards



Source: QH

CPCS Transcom International Limited projects an increase in railway traffic on the current network—which includes RVR, Tanzania Railway Limited (TRL), and Tanzania-Zambia Railway Authority (TAZARA)—driven by the economy's growth at a 6% CAGR over the next ten years. Railway capacity is seen growing from 3.7mn tonnes in 2007 to +16mn tonnes by 2030. The growth in rail volume will be partially driven by GDP growth and by attracting traffic from other transportation modes, mainly roads. A portion of road traffic is expected to be diverted to rail due to cost efficiency and potentially faster service upon completion of RVR's expansion program. Although we acknowledge that lower global oil prices would reduce the relative cheapness of rail. We value the company using the discounted cash flow methodology based on the inputs shown below. We note that lower global oil prices should have a neutral net effect on the company, because while volume growth may slow as heavy road transport becomes less expensive—as diesel prices are fully liberalised in Kenya and Uganda—the company's costs will fall, having a neutral impact on EBITDA. Fuel costs, as shown below, average 50% of the company's operating cash costs.

Key operating assumptions for RVR

	2014e	2015e	2016e	2017e	2018e	2019e
Cargo capacity (mn tonne km)	1,200	2,400	2,400	2,400	2,400	2,400
Operating rate (%)	100	80	100	100	100	100
Volumes transported (mn tonne km)	1,280	1,531	1,960	2,470	3,030	3,636
Fees per passenger (USD per NTK)	0.07	0.07	0.07	0.08	0.08	0.08
y-o-y growth (%)	20	2	2	2	2	2
Gross revenues (USDmn)	100	116	152	195	241	296
Concession fee (USDmn)	11	13	17	22	27	33
Net revenues (USDmn)	89	103	135	173	215	263
EBITDA (USDmn)	30	32	51	72	94	123
EBITDA margin (%)	33.8	31.1	37.6	41.5	43.8	46.7
Cost breakdown						
Fuel (USDmn)	30	40	51	63	77	81
Fixed costs (USDmn)	21	24	26	30	33	37
Personnel costs (USDmn)	37	39	45	52	55	57
Total (USDmn)	70	83	100	118	137	147
Cash cost per passenger (USD per NTK)	0.05	0.04	0.04	0.04	0.04	0.04

Source: QH, CI Capital estimates

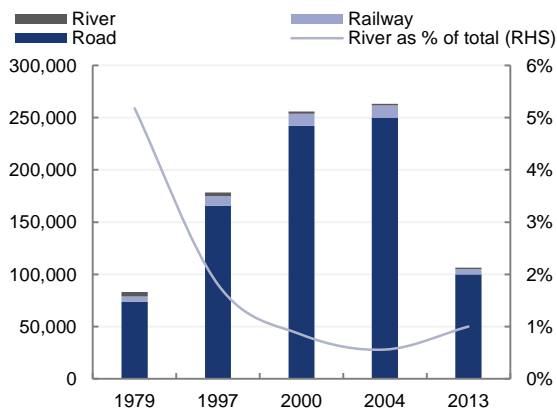
Nile Logistics

Nile Logistics (NL), 100%-owned by QH, is Egypt's main player in river transport, holding a 50% share of the country's total river transport market over 2011-13. NL offers river transport services and port management/operations in Egypt, North Sudan, and South Sudan, with a handling capacity of c2mn tpa.

River transport in Egypt should gain relative attractiveness as fuel subsidies are removed

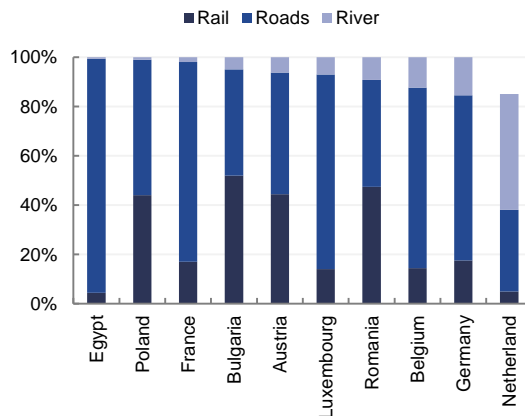
Cargo transportation via river currently represents a minimal c0.5% of total cargo transported across Egypt (2013: c380mn tonnes), while road transportation captures the lion's share with 96% of total goods transported across the country. Our view is that the river route will become increasingly popular over the coming period thanks to its fuel efficiency in a rising energy price environment. To put this into perspective, with 5 litres of fuel, a tonne can be carried over a distance of 550km using river barges but only 100km using the conventional trucking method. The recent move by the Egyptian government to implement a long awaited fuel subsidy restructuring, has rendered this route increasingly interesting. In July 2014, gasoline prices were hiked 78% on average, having serious repercussions on road transportation costs. On our numbers, total cargo transport across Egypt is set to grow at a CAGR of 6% p.a. in 2013-20, equivalent to an average 1.7x CI Capital's GDP growth estimates. River transportation should gradually start to gauge more market share as a highly rated alternative to the conventional trucking. Although historically, the ease and speed of road transport, as well as its relatively modest cost structure has incentivised companies, farmers, and traders to choose it over river, we think the sector will see structural changes over the coming years. That said, we look for a market share of 1% out of estimated total cargo transport of 566mn tonnes by 2020. This is relatively conservative, still well below the global market average of 11% market share for river transport. Needless to say, the major catalyst would be sharp energy subsidy reductions, given that fuel represents only c20% of the total river transport costs compared to an estimated 40% for trucking.

Historic split across modes of transport in Egypt



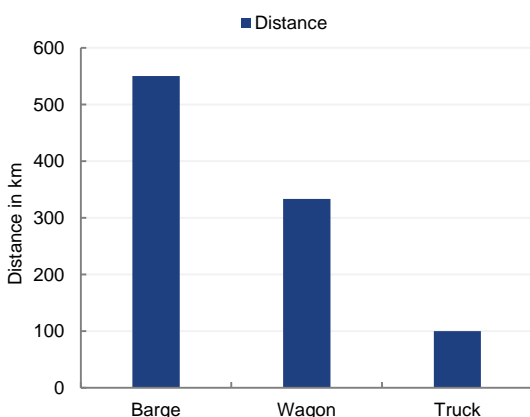
Source: River Transport Authority

River transport vs. other modes in select countries



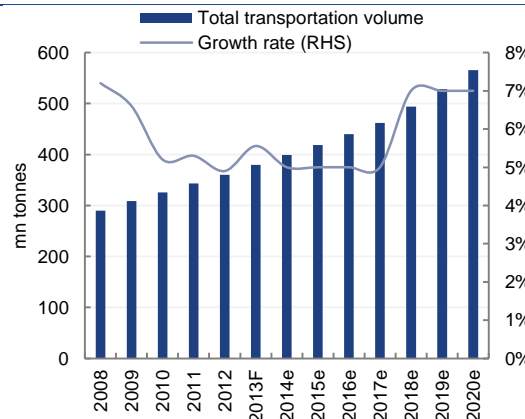
Source: QH, CI Capital

Fuel efficiency, measured by distance per 5 litres



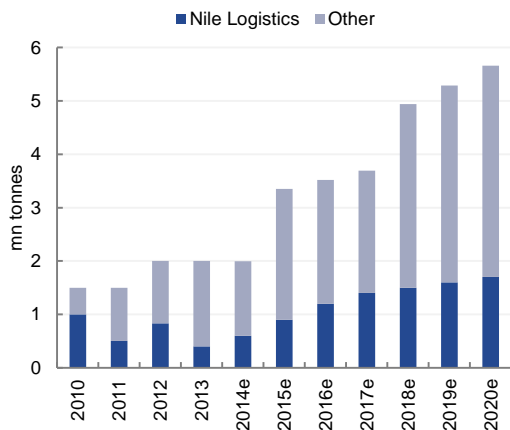
Source: QH, Industry reports, CI Capital estimates

Egypt cargo transport market volume



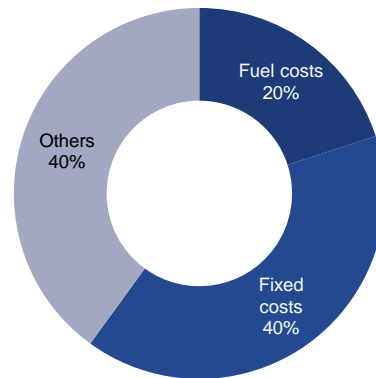
Source: QH, CI Capital estimates

Projected river cargo transport volume in Egypt



Source: QH, Industry reports, CI Capital estimates

Nile Logistics operating costs breakdown



Source: QH

In addition to the demand side, Egypt is also trying to encourage increased movement of goods (and passengers) through the river. In 2010, the Ministry of Transportation presented findings from its three-year Misr National Transport Study (MiNTS), explaining that river transport as a share of total cargo transport volume has plunged over the past 30 years; from 2007-13 alone, its levels plummeted from 5% to 0.5%—partially due to the limited regulations governing truck transportation. The MiNTS study forecasts that without any policy changes, river transport volumes will constitute around 1% of a predicted 900mn tonnes in total cargo by 2027. It is the government's stated long-term objective to phase out trailer trucks in Egypt to reduce the traffic and high accident rate. In August 2015, the government will implement a new law concerning trailers and the weights permitted to handle by trucks, according to the Ministry of Transportation. This law should incentivize the move towards a different transport mode.

Forecasts

Thanks to the 67% hike in diesel prices last June, and expectations for more stringent regulations governing heavy road transport (limiting driving hours to night time), we believe Nile Logistics will be able to significantly ramp-up its operating rates from 50% to at least 70% by 2018. Based on these fee assumptions and a gradual ramp-up in the company's operating rate to 85% in 2020e from c20% in 2013, which in turn should lead to proportional cost savings, we look for an EBITDA margin of 35% in 2020e.

Key operating assumptions for Nile Logistics

	2014e	2015e	2016e	2017e	2018e	2019e	2020e
Total Egypt cargo (mn tonnes)	399	419	440	462	494	529	566
y-o-y growth (%)	5.0	5.0	5.0	5.0	7.0	7.0	7.0
of which Nile transport	0.5	0.8	0.8	0.8	1.0	1.0	1.0
Nile transport (mn tonne)	2.0	3.4	3.5	3.7	4.9	5.3	5.7
Revenue (EGPmn)	62	266	338	373	401	430	459
EBITDA (EGPmn)	(37)	29	93	117	131	146	160

Source: QH, Industry reports, CI Capital estimates

Consolidated financials: Qalaa Holdings

EGPmn FY Dec	2014e	2015e	2016e	2017e	2018e		2014e	2015e	2016e	2017e	2018e
P&L						Basic data					
Revenue	6,386	8,867	10,997	27,175	36,314	Market cap	3,444	3,444	3,444	3,444	3,444
CoGS	(4,718)	(6,602)	(8,220)	(20,012)	(26,887)	Equity value ¹	5,444	5,444	5,444	5,444	5,444
Gross profit	1,250	1,826	2,314	6,378	8,623	EV	17,750	22,840	25,450	23,897	20,556
G&A	(1,123)	(1,181)	(1,237)	(1,315)	(1,404)	EPS (EGP)	(0.4)	(0.0)	0.2	0.7	1.0
EBITDA	651	1,118	1,636	5,984	8,165	DPS (EGP)	0.0	0.0	0.0	0.0	0.0
D&A	(418)	(439)	(462)	(784)	(803)	BV (EGP)	2.8	2.8	3.0	3.7	4.7
EBIT	233	679	1,173	5,200	7,362	FCF (EGP)	0.1	0.2	0.3	0.9	1.1
Net interest	827	725	689	933	1,289	Valuation					
P/BT	(835)	(46)	485	4,266	6,073	P/E (x)	(9.2)	(264.2)	19.1	4.6	3.3
FX	(91)	-	-	-	-	P/B (x)	1.2	1.2	1.2	0.9	0.7
Taxes	(54)	-	(145)	(1,067)	(1,518)	Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Minority	(295)	(25)	55	2,011	2,903	FCF yield (%)	3.3	7.0	9.5	27.7	32.4
Net income	(595)	(21)	284	1,189	1,652	EV/revenue (x)	2.8	2.6	2.3	0.9	0.6
Balance sheet						EV/EBITDA (x)	27.3	20.4	15.6	4.0	2.5
Cash	1,880	2,260	2,776	4,283	6,049	Growth					
Receivables	1,774	2,340	2,444	6,416	8,574	Revenue (% y-o-y)	32.9	38.8	24.0	147.1	33.6
Inventory	1,284	1,369	1,688	4,044	5,384	EBITDA (% y-o-y)	n/m	71.7	46.3	265.9	36.4
Investments	3,068	3,068	3,068	3,068	3,068	EBIT (% y-o-y)	n/m	191.7	72.8	343.2	41.6
Current assets	9,201	10,232	11,171	19,007	24,270	EPS (% y-o-y)	n/m	n/m	n/m	317.9	38.9
PP/E	2,767	2,807	2,641	2,475	2,309	Profitability					
Intangibles	3,663	3,663	3,663	3,663	3,663	RoE (%)	(13.3)	(0.5)	6.0	20.1	21.8
Non-current assets	28,165	34,660	39,038	40,488	40,254	RoA (%)	(1.6)	(0.0)	0.6	2.0	2.6
Total assets	37,366	44,892	50,209	59,495	64,524	RoC (%)	(3.2)	(0.1)	1.0	4.2	5.8
Payables	5,136	7,236	9,165	17,331	22,306	Gross margin (%)	19.6	20.6	21.0	23.5	23.7
Current liabilities	9,710	11,730	13,578	21,664	26,560	EBITDA margin (%)	10.2	12.6	14.9	22.0	22.5
LTD	13,857	19,407	22,614	22,648	21,153	Net margin (%)	(9.3)	(0.2)	2.6	4.4	4.5
Non-current liabilities	23,192	28,719	31,904	31,915	30,396	Liquidity					
Total liabilities	32,903	40,449	45,482	53,579	56,956	EBITDA/interest (x)	0.8	1.5	2.4	6.4	6.3
Owner equity	4,463	4,442	4,727	5,916	7,567	ND/equity (x)	3.2	4.4	4.7	3.5	2.3
Cash flow						ND/assets (x)	0.4	0.4	0.4	0.3	0.3
Cash from operations	1,301	1,844	2,229	3,788	3,910	ND/EBITDA (x)	22.0	17.4	13.5	3.4	2.1
Capex	(7,521)	(6,933)	(4,840)	(2,235)	(569)	Current ratio (x)	0.9	0.9	0.8	0.9	0.9
Cash from investing	(7,521)	(6,933)	(4,840)	(2,235)	(569)	Quick ratio (x)	0.8	0.8	0.7	0.7	0.7
Cash from financing	6,400	5,470	3,127	(46)	(1,576)						
FCF	181	380	516	1,507	1,765						

Source: Company financials, CI Capital estimates

Notes: Based on 8 Jan 2015 closing.

Note 1: All multiples and yields are calculated based on the equity value for QH, which reflects the market cap and the value of preferred shares.

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