BRES Alert – 2Q2018 Adjusted Net Income Misses; Maintain Accumulate

- **BRES posts softer-than-expected results with headline profit beat due to one-offs –** Barwa Real Estate Company's (BRES) net profit declined 7.8% YoY (-1.5% QoQ) to QR398.8mn in 2Q2018. We were expecting 2Q2018 net income of QR240.1mn. However, stripping out QR256.2mn in one-offs for the quarter (primarily due to QR88.1mn in FV gains on investment properties and QR140.4mn in gain on debt restructure), adjusted net profit came in at QR142.6mn; adjusted net income dropped 31.9% YoY and fell 19.0% QoQ. Reported EPS amounted to QR1.03 in 2Q2018 as compared to QR1.11 in 2Q2017 and QR1.04 in 1Q2018.

- **Revenue marginally softer-than-expected but increased costs pressure margins.** The company's rental income came in at QR321.2mn in 2Q2018 (our estimate: QR359.4mn), which represents an increase of 5.4% YoY. However, on QoQ basis, rental income declined 5.3%. Recurring revenue of QR405.0mn (which includes rental, consultancy and finance lease revenue) increased 0.7% YoY but declined 6.0% QoQ and was 4.1% below our estimate of QR422.1mn. Moreover, direct costs increased 11.9% YoY/3.1% QoQ and was 29.4% ahead of our estimate. Consequently, gross margins slipped to 61.6% in 2Q2018 vs. 65.5% in 2Q2017 and 65.0% in 1Q2018. Moreover, income from associates dropped from QR36.1mn in 2Q2017 to QR11.8mn in 2Q2017.

- **BRES's position within Qatari real estate supports growth.** BRES targets the low-to-mid end of the market but is transitioning into the mid-to-higher end with Lusail Dara B-F (design phase). This fits into our view of higher demand for that segment given our outlook on the Qatari economy by 2022. Note that BRES is 45% owned by Qatari Diar, which could prove a backstop in case of need to refinance/fund growth.

- **We maintain Accumulate/QR39 price target.** Upcoming catalysts include: Mawater phase II (3Q18); Lusail Dara A (3Q18); Barwa Village expansion (3Q18); and Barwa Al Baraha warehouses (2Q19); Salwa Labor City (2Q19).

- **Risks to thesis:** Dividend sustainability. Ability to re-profile debt at comparable cost. Ability to secure funding for organic/acquisitive growth.

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Recommendations *Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price*	
OUTPERFORM	Greater than +20%
ACCUMULATE	Between +10% to +20%
MARKET PERFORM	Between -10% to +10%
REDUCE	Between -10% to -20%
UNDERPERFORM	Lower than -20%

Risk Ratings *Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals*	
R-1	Significantly lower than average
R-2	Lower than average
R-3	Medium / In-line with the average
R-4	Above average
R-5	Significantly above average

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