

VFQS Alert – Modest Miss in 3Q2022 Earnings But Thesis Stays Intact; Accumulate

- **VFQS delivers another strong quarter with 3Q2022 net profit of QR118.1mn (78.0% YoY, 8.4% QoQ) that, however, missed our forecast of QR124.6mn by 5.2% on lower-than-expected cash gross margin – Quarterly revenue of QR740.2mn (27.0% YoY, 4.9% QoQ) was just 2.8% shy of our estimate of QR761.6mn. While we do not have full details, the company’s reported QR1.9bn in 9M2022 service revenue (mobile + fixed), up ~14.2% YoY, was just a little bit below our forecast. This could imply that revenue from other segments, including equipment, handsets, hardware revenue associated with project build-outs, etc., were also moderately below our estimate.**
- **Vodafone Qatar also reported mobile subs of roughly 2.1mn, which was lower than our forecast of 2.2mn. Mobile subs expanded 14.9% YoY vs. 1.8mn in 3Q2021 and were up ~2.5% vs. 2.0mn in 2Q2022. This exceeded the 13.2% yearly growth in Qatar’s population in 3Q2022 but fell below its significant 12.3% QoQ increase.**
- **Higher-than-expected cash interconnection and other direct costs, along with the above mentioned top-line miss, contributed to the miss in 3Q2022 earnings. Cash gross margin came in 64.5% in 3Q2022 (vs. our estimate of 67.0%) and 3Q2021’s 68.3% and 2Q2022’s 67.2%. Gross profit of QR477.4mn (20.0% YoY, 0.7% QoQ) was 6.5% below our forecast of QR510.4mn.**
- **Reported 3Q2022 EBITDA margin of 39.0% was lower than 42.7% in 3Q2021 and 41.0% in 2Q2022. We were forecasting an EBITDA margin of 41.0% in 3Q2022. Quarterly EBITDA of QR288.5mn grew 16.0% YoY but was flattish (down 0.3%) QoQ and was below our estimate of QR312.4mn (7.7% divergence). For the YTD period, reported EBITDA margin declined from 41.3% in 9M2021 to 40.4% in 9M2022 given a higher mix of comparatively lower-margin projects revenue.**
- **Our view on the stock remains unchanged – we continue believe the upcoming FIFA World Cup Qatar 2022 could act as a potential boost to 2H2022 (especially 4Q2022) results. The company’s stock price has been in a dead zone this year, down 1.7% vs. its competitor Ooredoo’s gain of 31.8%. While ORDS has enjoyed its own unique set of drivers this year, we believe VFQS’ underperformance could reverse going forward as we get closer to the World Cup. Growth in 2H2022 results could be key in driving near-term stock price. Further clarity provided by management on the potential impact of 1+mn World Cup visitors on VFQS’ operations, should also help provide a catalyst. Longer-term, we also believe postpaid (68.9% of 1H2022 mobile service revenue), 5G, fixed, broadband, enterprise and bundled ICT solutions should boost growth. While capex levels remain elevated due to 5G and coverage/capacity expansion ahead of the WC, dividend and FCF yields should improve going forward. We maintain our Accumulate rating on VFQS shares and our price target of QR1.950.**

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INCOME STATEMENT		3QCY21 A	2QCY22 A	3QCY22 A	3QCY22 E	A Vs. E	YoY	QoQ
<i>(In QR mn Unless Specified)</i>								
Revenue		582.749	705.329	740.173	761.605	-2.8%	27.0%	4.9%
	<i>YoY Growth (%)</i>	8.0%	22.1%	27.0%	30.7%			
Direct Costs (Interconnection & Other Opex)		(184.936)	(231.248)	(262.725)	(251.222)	4.6%	42.1%	13.6%
	<i>as a % of Total Revenue (%)</i>	31.7%	32.8%	35.5%	33.0%			
Gross Profit (Loss)		397.813	474.081	477.448	510.384	-6.5%	20.0%	0.7%
	<i>Gross Margin (%)</i>	68.3%	67.2%	64.5%	67.0%			
Other Expenses (Employee and Other Expenses)		(149.241)	(184.718)	(188.996)	(198.017)	-4.6%	26.6%	2.3%
	<i>as a % of Total Revenue (%)</i>	25.6%	26.2%	25.5%	26.0%			
Depreciation and Amortization		(170.076)	(157.093)	(148.480)	(163.582)	-9.2%	-12.7%	-5.5%
Total Operating Expenses		(319.317)	(341.811)	(337.476)	(361.600)	-6.7%	5.7%	-1.3%
EBITDA		248.572	289.363	288.452	312.366	-7.7%	16.0%	-0.3%
	<i>EBITDA Margin (%)</i>	42.7%	41.0%	39.0%	41.0%			
Operating Profit (Loss) - EBIT		78.496	132.270	139.972	148.784	-5.9%	78.3%	5.8%
	<i>EBIT Margin (%)</i>	13.5%	18.8%	18.9%	19.5%			
Interest Income		1.049	1.704	1.575	1.750	-10.0%	50.1%	-7.6%
Interest Expense/Lease Interest Expense		(4.519)	(11.960)	(10.474)	(11.030)	-5.0%	131.8%	-12.4%
Other Income/Expense		(8.692)	(13.054)	(13.008)	(14.925)	-12.8%	49.7%	-0.4%
Profit (Loss) Before Tax		66.334	108.960	118.065	124.579	-5.2%	78.0%	8.4%
Net Profit (loss) - Adjusted		66.334	108.960	118.065	124.579	-5.2%	78.0%	8.4%
	<i>Net Margin (%)</i>	11.4%	15.4%	16.0%	16.4%			
EPS (QR)		0.02	0.03	0.03	0.03	-5.2%	78.0%	8.4%

Recommendations		Risk Ratings	
<i>Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price</i>		<i>Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals</i>	
OUTPERFORM	Greater than +20%	R-1	Significantly lower than average
ACCUMULATE	Between +10% to +20%	R-2	Lower than average
MARKET PERFORM	Between -10% to +10%	R-3	Medium / In-line with the average
REDUCE	Between -10% to -20%	R-4	Above average
UNDERPERFORM	Lower than -20%	R-5	Significantly above average

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