المجموعة المالية - هيرميس
EFG HERMES

GCC SHIPPING SECTOR

Regional Resilience

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CONTENTS

- **The Outlook For the Shipping Industry Appears Bleak**, with some leading indicators falling more than 90% since they peaked only in mid-2008. Demand is plummeting and at the same time supply is growing at record levels. Perversely, it seems, that after enjoying unprecedented growth in recent years, the industry is about to enter the most difficult period in its history.

- **We Expect the Market to Remain Difficult in 2009 Forcing Many Operators to Simply Go Out of Business**. This should lead to a capacity reduction as a large portion of the orderbook is cancelled. Also, further supply restriction will be imposed as the industry consolidates over the next year. Overall, our forecasts are factoring a bottoming in the market in 2009 and a small improvement in 2010/2011.

- **Despite the Doom and Gloom, We Believe There are Attractive Opportunities Within the Sector, Specifically in the MENA Region**, as it has higher exposure to crude oil, which should be more resilient in the downturn. For example, VLCC (crude) tanker rates have fallen back nearer to their 2007 levels, whereas Dry bulk is trading at 93% below the 2007 daily rate. In fact, a significant portion of the industry weakness is in areas where the MENA ship owners have low exposure – specifically Dry Bulk and Containers. In addition, it is worth emphasising that most MENA ship owners have their ships on charter and are not exposed to the volatile and weak spot market. Consequently we expect the region to outperform in the current cycle.

- **Overall, We Favour Stocks With** a) significant revenue visibility, b) low short-term exposure to the spot market, c) exposure to crude oil d) strong balance sheets.

- **Our Top Picks are Qatar Shipping and Qatar Navigation** and we initiate with ST/ LT Buy recommendations on both stocks with price targets of QAR34.4 for QShip and QAR82.3 for QNav, implying upside of 46% and 50% respectively. Also our SOTP market cap value target for the merged entity stands at QAR9.3 billion implying 58% upside as we believe the merger will offer significant synergies.

- **We Initiate on Nakilat with a ST Neutral and LT Accumulate Recommendation with a Price Target of QAR19.6** – implying 32% upside as we believe the company is likely to be the most defensive shipping stock given the strong revenue visibility provided by the long-term charter contracts. However, we remain cautious in the short term due to uncertainty on the LNG projects and vessel rates.

- **We Initiate on Gulf Navigation with a ST Accumulate and LT Neutral Recommendation and AED0.77 Price Target** implying 38% upside as we suspect the group could become a consolidation target at some point in 2009.

- **We Initiate on National Shipping Company of Saudi Arabia (NSCSA) with a ST Sell / LT Neutral Recommendation and a Price Target of SAR14.9 Implying 15% Downside.** The group has significant scale and a strong management team but with 60% of the fleet exposed to the spot market and a large orderbook, we suspect newsflow could get worse before getting better and consequently we remain cautious in the near term

SECTOR NOTE

Companies Analysed in this Report

	Currency	Price	LTFV	Upside/ Downside %	Recommendation ST	LT	M. Cap. mn	P/E 2009e	2010e	P/B 2009e	EV/ EBITDA 2009e
Qatar Navigation	QAR	54.9	82.3	50%	Buy	Buy	4,290	6.6	5.6	0.5	8.6
Qatar Shipping	QAR	23.6	34.4	46%	Buy	Buy	3,971	5.7	4.7	0.5	7.8
Gulf Navigation	AED	0.56	0.77	38%	Accumulate	Neutral	1,208	8.5	7.0	0.6	7.1
Nakilat	QAR	14.8	19.6	32%	Neutral	Accumulate	8,200	7.1	4.5	2.0	22.3
NSCSA	SAR	17.6	14.9	-15%	Sell	Neutral	5,544	12.7	10.3	1.1	7.2
M. Cap Weighted Avg.					.			8.0	6.4	0.7	7.8

**Prices as at26 January 2009*

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EXECUTIVE SUMMARY

Outlook appears difficult

The outlook for the shipping industry appears bleak, with some earnings indicators falling more than 90% over the last six months. For example, the BDI has dropped 97% since its peak and the broader earnings indicator, the Clarksea Index, has lost 78% since it peaked in 2008.

This rapid decline is due to a combination of weakening demand, particularly from China, and a record orderbook, which suggests that the size of the world vessel fleet is expected to rise by more than 50% in the next three years.

Expect orderbook cancellations to accelerate

We expect the market to remain difficult in 2009 but the current orderbook is simply unsustainable in our view, as many operators are running out of cash and will not be in a position to take delivery of ships. As a result, we expect to see the rate of orderbook cancellations to increase markedly during the course of the year. In addition, industry consolidation is expected to accelerate, which should result in further supply cuts. Consequently, we suspect daily rates could stabilise in the 2H of the year.

Demand should pick up when credit facilities ease

The demand side is more difficult to gauge. However, we believe demand has been unnaturally suppressed due to the credit crunch as many banks have withdrawn credit facilities resulting in some ship operators refusing to deliver goods they believe the recipient may not be in a position to pay for in full. This fear factor and the lack of confidence has put further pressure on daily rates. On a brighter note, Fearnleys has reported that activity in the market has picked up marginally since the start of the year, and while it is too early to suggest a recovery, we do expect some increase in demand as and when banking facilities return to somewhere near normal levels.

Ship operator's performance will depend on exposure to spot market / industry sub sectors

While the overall market may be currently depressed, a ship owner / operator's performance depends on exposure to a) spot market and b) industry sub sectors. For example, vessels exposed to the spot market would have seen income fall between 50% and 90% in the last six months, while chartered ships have no market exposure unless the contract is up for renewal. That said, we have seen some charter contracts being cancelled or renegotiated, particularly in the dry market.

In addition to the above, vessels rates vary sector to sector. For instance, while the price of crude oil has been volatile, the demand and supply of oil is relatively inelastic. Currently, the daily rate for a VLCC is cUSD60k – still significantly below the 2008 peak of USD220k but higher than the 2007 average of USD55k. In contrast, the dry bulk sector is expected to remain extremely difficult for the foreseeable future as the construction boom in China / India has slowed significantly. The daily rate for a large dry carrier currently stands at USD7k – 97% below its 2008 peak of USD220k and 93% below the 2007 average of USD95k. Overall, a ship operator could significantly outperform the market in a downturn depending on fleet type and strategy.

MENA shipping industry well placed to benefit in long term

The MENA shipping industry plays a significant role in the market due to its geographic position in the trade route between Asia and Europe. In addition, the region's operators have close relationships with large natural resource producers, which offers a competitive advantage. Furthermore, the entire MENA shipping industry has undertaken a large capex programme in the last few years to upgrade all its infrastructure from natural resource production facilities, cargo / handling operations, to modern state of the art vessels. Consequently, the region should be in a strong position to benefit from the long-term growth of the industry.

MENA ship operators should outperform

In relation to the current downturn, we expect the MENA operators to outperform on a relative basis due to their higher exposure to crude oil. Ownership of dry bulk and container vessels is limited. More significantly, most operators have the bulk of their fleet on charter (short, medium and long term) and have limited exposure to the current spot market. Consequently, earnings in the short term are expected to hold up, and it is worth emphasizing that most operators chartered their ships before the spike in 2008, and are unlikely to see rates dropping significantly on a like-for-like basis when contracts are renewed.

Overall, the EFG MENA Shipping Index declined 39% in 2008, in line with the global shipping industry. However, we believe some shares have fallen too far and now offer good value. Below we highlight our key recommendations:

Qatar Shipping and **Qatar Navigation** are merging with a view to improving profitability and we believe there could be significant cost synergy opportunities. The core shipping business has its vessels on charter and most of its exposure is in Qatar, which is expected to remain one of the most resilient economies in the region in the current downturn. In addition, the group owns many non-core businesses that could be divested to advance shareholder value. Furthermore, the group has a combined 30% stake in Nakilat, which accounts for 42% of the group's current market cap. We estimate that Nakilat is currently undervalued by 32% and this offers further upside potential. Excluding the Nakilat stake, the stock trades on 3.0x 2009e earnings, which is unfair in our view given the long-term growth potential of the business. Overall, we believe the current share prices offer an attractive entry point and we initiate on Qatar Shipping and Qatar Navigation with ST/ LT Buy recommendations with a price target of QAR34.4 for QShip and QAR82.3 for QNav. Also our market cap price target for the merged entity stands at QAR9.3 billion.

Nakilat is an LNG fleet operator out of Qatar and is expected to own 54 LNG vessels by 2010. Nakilat has long-term charter contracts (approximately 25 years) with LNG producers Rasgas and Qatargas. In theory, the group has 100% revenue visibility with no exposure to the spot market. However, in the short term, the group is reliant on the timely delivery of all its vessels and the completion of the LNG production facilities. That said, to date, the vessels have all been delivered on schedule and we expect Nakilat's business to remain resilient. We believe risks to our forecast weigh on the upside which should mean there is room for upgrades to our fair value target of QAR19.6 once revenue visibility improves. We initiate on Nakilat with a ST Neutral, LT Accumulate rating.

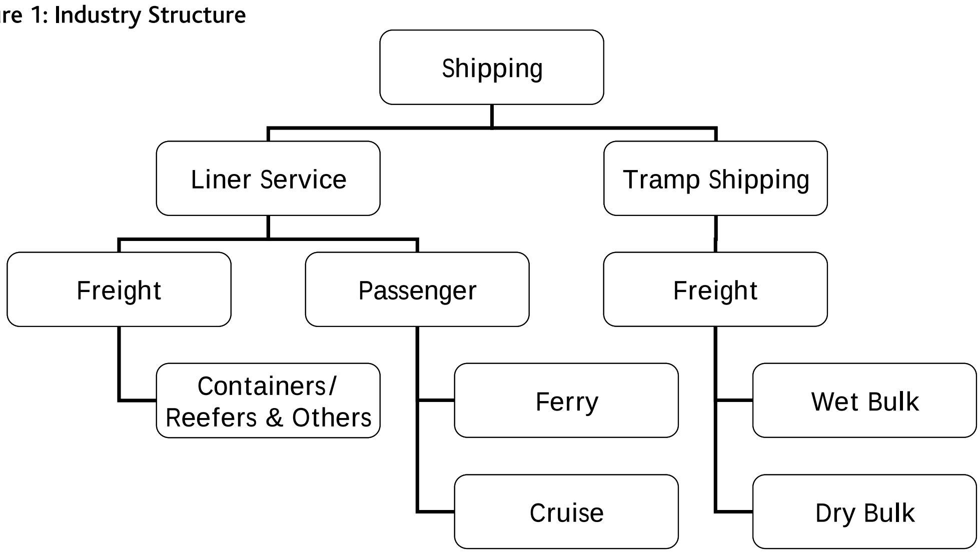
Gulf Navigation was floated in 2003 with a view to becoming a major ship operator with an aggressive expansion strategy. However, the subsequent steep increase in vessel acquisition costs meant Gulf Nav was unable to execute its plan. At the end of 2009e, the group will operate 14 vessels, as opposed to the 29 that were mooted at the IPO. Going forward, we expect 2009 to be a difficult year as we estimate the group has renewed five vessel contracts in the last quarter at 20% below the previous agreements. Consequently we are forecasting an EPS decline of 32% in 2009e but, despite this, we believe the dividend can be maintained, which currently yields an attractive 12.3%. In addition, the announced 10% share buy-back programme is likely to be 11% EPS accretive at the current share price, which could further boost the shares. Furthermore, we believe Gulf Nav could be a primary target for consolidation as it lacks scale to become a major industry player. With this in mind, we initiate Gulf Navigation with ST Accumulate / LT Neutral recommendation.

NSCSA (National Shipping Company of Saudi Arabia) is one of the largest vessel operators in the region with exposure to container, LPG, petrochemicals and oil tankers. The group has an experienced management team and a solid track record. NSCSA has enjoyed strong earnings growth in recent quarters as it is highly exposed to the spot market (c.60% of fleet). As a result earnings grew by 59% in 2008 but, with the spot market plummeting, we estimate that earnings will fall by 41% in 2009e. More worryingly, NSCSA is due to take delivery of 16 chemical carriers and four VLCCs in the next two years and none of these vessels have been pre-chartered, which means that its exposure to the spot market is likely to rise significantly. Overall, in the long term, we expect NSCSA to weather the current downturn as we believe the group receives attractive funding from the local banks but we remain cautious in the near term due to the volatility within the spot market. As a result, we initiate with ST Sell and LT Neutral recommendation.

I. BACKROUND

The roots of the shipping industry can be traced back to c.1500 BC. However, the shipping revolution truly arrived in the 19th century when the first liner service was launched on January 1818. Today, despite the advancement of other forms of travel, 90% of all goods are still transported by sea.

Figure 1: Industry Structure



Source: EFG-Hermes

The shipping industry can be split between liner and tramp shipping. Liner service runs on a regular timetable transporting freight or passengers. Tramp shipping refers to on-demand transportation, usually oil or dry raw materials. In practice, three sectors dominate the market; Wet, Dry and Container, with Wet and Dry estimated to account for c. 30% each, and Container accounting for a further 12%.

The wet market refers to the transportation of liquids such as oil, gas and chemicals. Dry bulk refers to raw materials such as grains, coal, ore, and cement. Containers typically transport manufactured goods.

Wet bulk is transported in tankers; Dry in dry bulk carriers and Containers in container ships.

a. **Tanker capacity is measured in DWT (dead weight tons)**. The key tanker types are (DWT): Panamax (60k-80k); Aframax (80k-120k); Suezmax (120k-200k); VLCC (200k-315k), ULCC (320k-550k). The most common tanker is the VLCC (Very Large Crude Carrier), which carries about 2mn barrels of oil.

b. **Bulk carriers are also measured in DWT and there are four main types:** Handysize (10k-35k), Handymax (35k-55k), Panamax (60k-80k), Capesize(>80k)

c. **Container capacity is usually expressed in twenty-foot-equivalent units (TEU)** i.e. the volume of a twenty-foot-long shipping container. A forty-foot unit is known as two TEUs. The largest container ships can carry up to 15,200 TEU.

THERE ARE FIVE CATEGORIES IN THE TRANSPORT CHAIN:

1. Cargo owners
2. Traders
3. Ship managers
4. Shipbrokers
5. Ship owners (shipping companies/operators)

Cargo owners have goods that need to be moved by sea, they may be primary producers such as oil companies or iron ore mines. Traders are similar to cargo owners but they purchase commodities on a speculative basis with a view to reselling them, often in a different location, so they become involved in the transport process. Ship managers undertake the management (both technical and commercial) of ships on behalf of ship owners, often for a fixed fee. The presence of ship managers makes it easier for new companies to enter the business as the core management tasks can be outsourced. A shipbroker is involved in ordering new ships; buying and selling existing ships; and negotiating charters for the vessel. Finally, ship owners lease their vessels either for a single journey in the spot market or under a charter for a long-term period.

TYPES OF CHARTERS

Voyage Charter (spot) refers to a single journey with the hiring of both vessel and crew. The charterer / cargo owner pays the vessel owner on a per-ton or lump-sum basis. The ship owner is responsible for the port, fuel and crew costs.

Time Charter refers to the hiring of a vessel for a specific amount of time. The charterer pays for all expenses except for crew costs.

Bareboat Charter is when the charterer takes complete control of the vessel including crew management. The ship owner is not responsible for any costs.

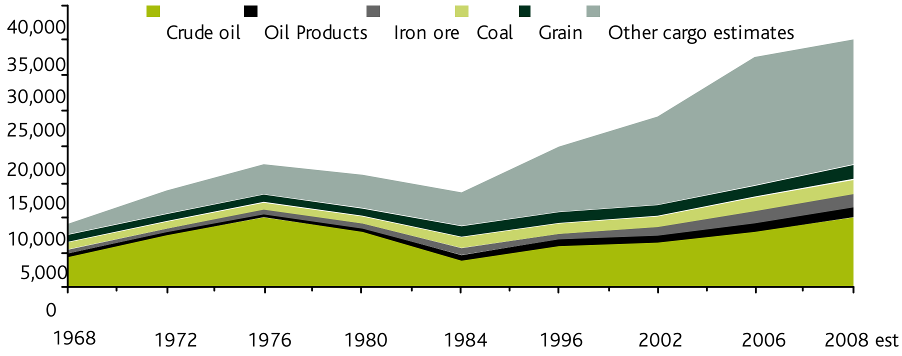
RECENT HISTORY

The Golden Era

Shipping is a cyclical industry, with its fortunes closely correlated to the health of the global economy as trade (import / export) activity tends to rise during expansionary periods and slows during recessionary times. Historically, a typical cycle lasted four years with two good and two bad years. But the recent cycle has been somewhat different, with the industry enjoying what can only be described as its golden era with unprecedented levels of sustained growth.

As Figure 2 illustrates, the growth in seaborne trade saw a steep change in 2002 when growth accelerated significantly. This is largely explained by the growth of emerging economies, most notably China and India. For example, China switched from being a net exporter of iron ore to net importer at the turn of the 21st century. This, combined with increasing trade between emerging economies, meant the seaborne business grew faster than global GDP.

Figure 2: Seaborne Trade
In DWT, unless otherwise stated



Source: Clarksons

GENERAL MARKET INDICATORS

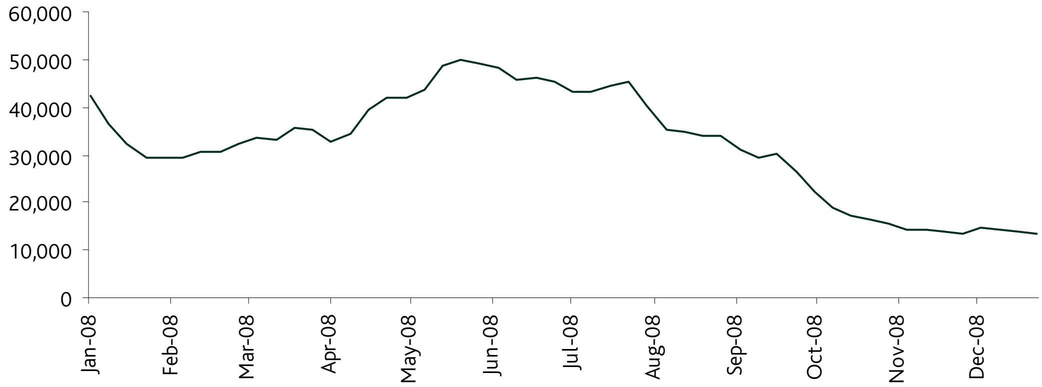
The Clarksea Index is a weekly indicator of earnings for all the main commercial vessel types and is a good proxy for the sector's health. Shipping freight rates are typically volatile as the supply side is fixed in the short term because it takes a few years to build a ship. Consequently a change in demand can lead to a material change in the freight rate.

Figure 3: Clarksea Index
In USD/Day, unless otherwise stated

Source: Clarksons

The Clarksea Index has been trading at record levels in recent years following the surge in cargo trade since 2002. The index spiked to 38,000 in 2004 as the ramp-up in demand took the market by surprise. The global economy continued to motor in 2005 driving the index to new levels of 43,000 before dropping off. The Clarksea Index reached new heights in 2007 and again in Q1 2008, but the picture has changed dramatically in recent months.

Figure 4: Clarksea 1 Year Performance: Declines to Near Historic Lows
In USD/Day, unless otherwise stated



Source: Clarksons

More recently, the index has fallen sharply from the peak of 49,742 reached in May 2008, to 10,701 in the beginning of January 2009, which is not a surprise given the concerns about the shape of the global economy. Furthermore, the credit crunch has a direct impact on the sector as the industry is heavily geared. For instance, the ship orderbook is currently at an all time high of 60% of existing fleet and many ship owner's existing funding facilities are being withdrawn, which suggests many planned projects may simply be cancelled. Even if funding becomes available, the drop in the freight rates means the return on investment is likely to be lower than previously anticipated.

SPECIFIC MARKET DRIVERS

While the Clarksea Index is a good indicator of the overall industry activity, in practice the three different sectors (Wet, Dry and Container) have their own individual drivers.

We will examine four key metrics for each sector:

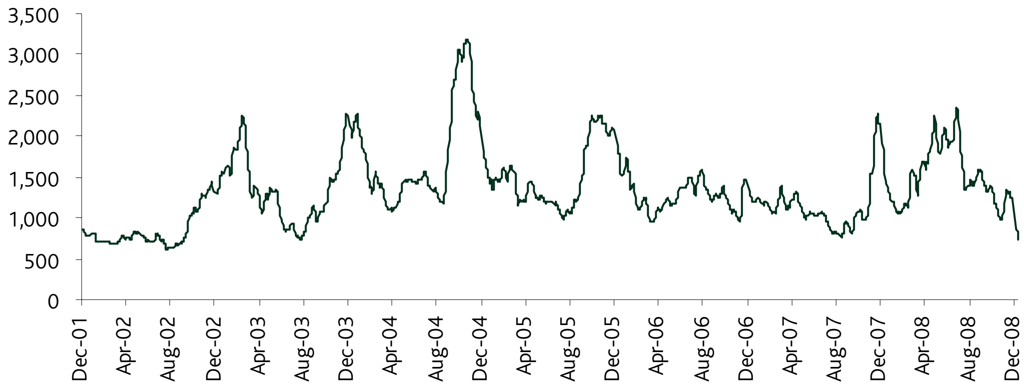
- Freight rates
- Orderbook
- Average age of fleet
- Second-hand prices

Freight rates typically highlight the level of short-term demand, while the orderbook offers an insight as to how the supply of vessels is likely to change. In our view, the orderbook needs to be examined alongside the age of the existing industry fleet to evaluate whether the increase in supply can be easily absorbed. For example, a large orderbook may not necessarily mean the fleet size will increase significantly as the existing fleet may be old and in need of scrapping, whereas if the fleet is relatively new then supply will most definitely increase. Finally, the second-hand prices offer an insight as to how the value of the ship owners fleet may have changed. This is useful, as shipping companies tend to value their fleet at net book value (cost less depreciation), and not at market value.

WET/TANKER

Tankers are used to transport liquid; mostly oil and their earnings capability is dependent on the level of demand for imported oil. We will use the Baltic Exchange Dirty Tanker Index as the earning indicator. The BDTI is the average of freight rates on the international tanker dirty (crude oil) routes

Figure 5: BDTI

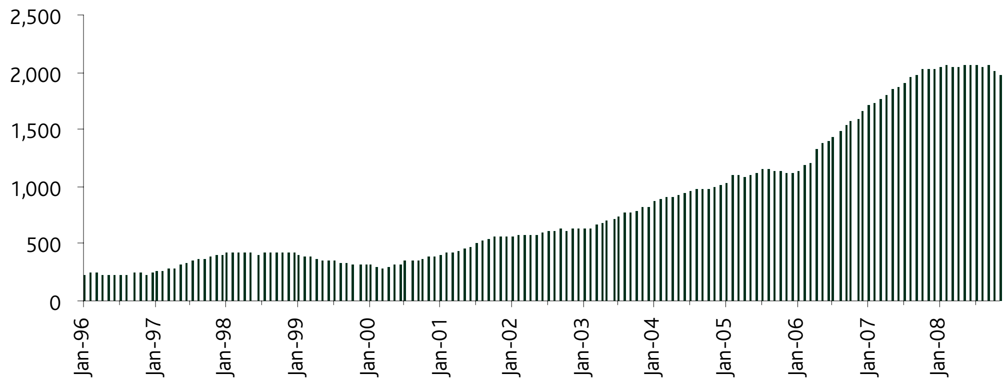


Source: Clarksons

As Figure 5 indicates, the BDTI has been volatile in recent years; peaking in 2004 as demand ramped up during a period when supply of vessels was short. Prices eased from the 2004 level but have been volatile since. More recently, prices have fallen sharply, which is again a reflection on the slowing global economy.

Supply Side of the Wet/Tanker Market

Figure 6: Tanker Orderbook
number of ships, unless otherwise stated



Source: Clarksons

The tanker fleet has grown at 5.4% CAGR over the last five years but the orderbook was ramped up in 2006 following the spike in earnings in the preceding months. Currently the orderbook stands at 45% of the existing fleet, which is a record.

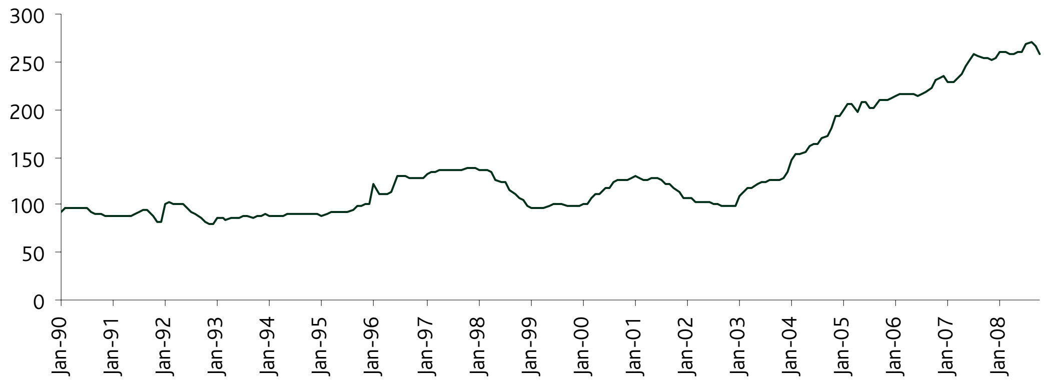
Figure 7: Age of Fleet: 28% of Fleet Older Than 15 Years

	% of Fleet <5 years	% of Fleet 5-9 years	% of Fleet 10-14 years	% of Fleet 15-19 years	% of Fleet >20 years
VLCC/ULCC	28	34	20	15.5	2.5
Suezmax	34	27.5	14	18.5	6
Aframax	38	24	12	16	10
Panamax	56	15	4	8	17
Total	39	21	12	11	17

Source: Clarksons

The age of the fleet, with 28% of the fleet older than 15 years, would suggest that the current orderbook is sustainable as much of the existing fleet is likely to be scrapped in the next five years. In addition, the rise in supply should be somewhat offset by a further increase in scrapping rates due to regulation, as the industry is required to phase out all single hull ships between 2010 and 2015. Currently, single hull ships account for circa 30% of the market (Clarksons) which means that a significant portion of the current fleet is heading for the scrapheap during the next seven years.

Figure 8: Tanker Second Hand Prices Index: A fall to Historic Lows Expected



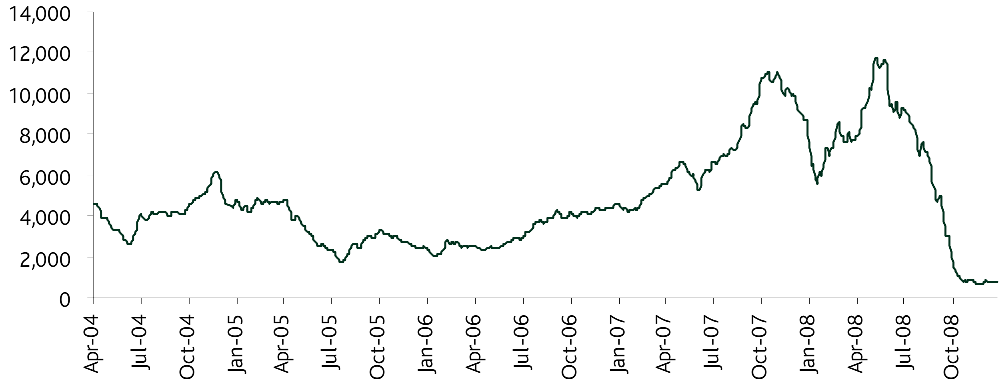
Source: Clarksons

Similar to the earnings index, the second-hand tanker market began to appreciate in 2004 and hit record levels in 2008. This was due to shipbuilding yards operating at full capacity. However, with freight rates dropping significantly, we would expect the second-hand index to also drop to near historic lows in the coming months. Due to the lack of transactions, the chart above is not reflective of current market conditions.

DRY

The dry sector is geared to the economic performance of developing economies such as China and India, which are key importers of raw materials. The key earnings indicator we use is the Baltic Dry Index (BDI), which calculates the average freight rates from 22 of the key global routes.

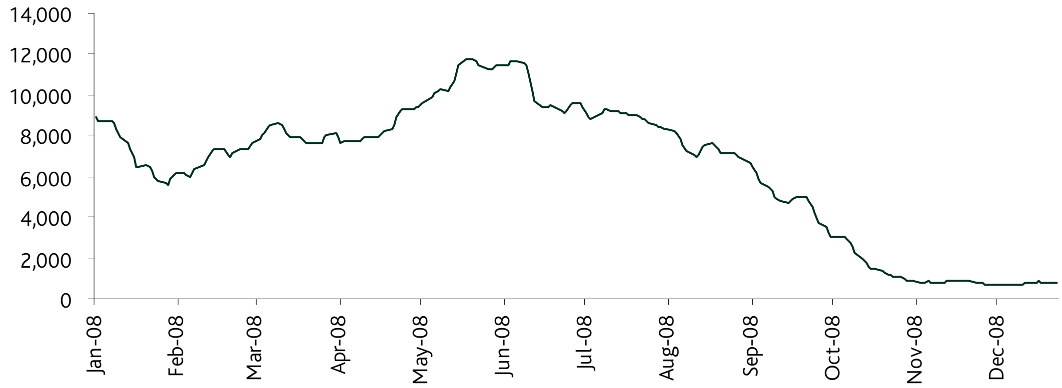
Figure 9: BDI 5 year Performance



Source: Clarksons

The BDI rose from 1600 in the March 2000 to above 6000 in May 2004 i.e. growth of >300%, before hitting 11,500 in March 2008. In absolute terms the BDI rose over 700% in the five years between March 2003 and 2008. The construction boom in China has driven the growth in dry bulk as China switched from being a net exporter of iron ore (used to produce steel) to a net importer in the 21st century. For example, China imported 70m tons of iron ore in the year 2000, but that was expected to rise to 460m tons by the end of 2008 – i.e. an absolute growth rate of 557% or a CAGR of 26%.

Figure 10: BDI 2008: A 97% Fall from the Peak in May 2008

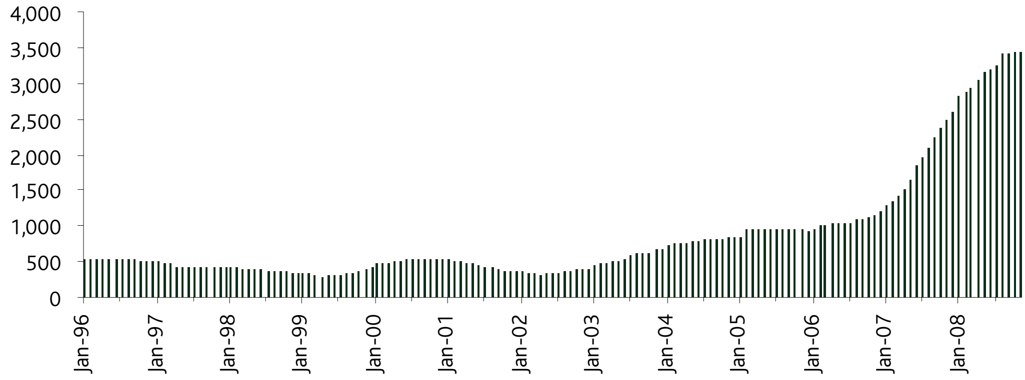


Source: Clarksons

The recent picture in the dry market has been somewhat different, however, with the BDI dropping 97% since its peak in May 2008. Concerns about the health of the global economy, with a particular focus on a likely slowdown in China, is weighing on the dry index.

Supply Side of Dry Bulk

Figure 11: Dry Orderbook
Number of ships, unless otherwise stated



Source: Clarksons

The supply side is another area of concern. Up until Q1 2007, the dry market had a relatively low orderbook but that changed over the course of 2007 and now it stands at 60% of the fleet. And, in fact, for the larger Capesize vessels, the orderbook stands at a worrying 90% of the current fleet.

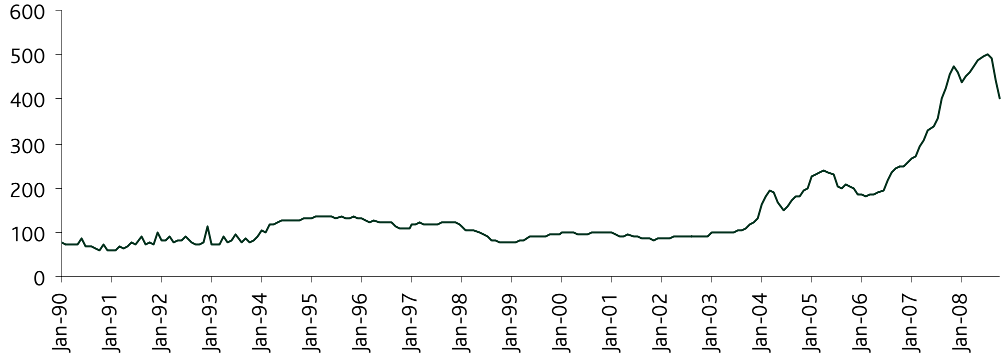
Figure 12: Age of fleet: 46% of fleet older than 15 years

	% of fleet <5 years	% of fleet 5-9 years	% of fleet 10-14 years	% of fleet 15-19 years	% of fleet >20 years
Handysize	12	10	13	4	61
Handymax	28	20	22	6	24
Panamax	27	21	19.5	8	24.5
Capesize	29	16	21	15	19
Total	21	16	17	7	39

Source:, Clarksons

Similar to the tanker market, the dry bulk fleet is relatively old with 46% more than 15 years old. This suggests the increase in capacity will not be as marked as the orderbook indicates, as a significant portion of dry vessels are likely to be scrapped in the next five years.

Figure 13: Dry second hand prices Index: Recent sharp falls likely to continue



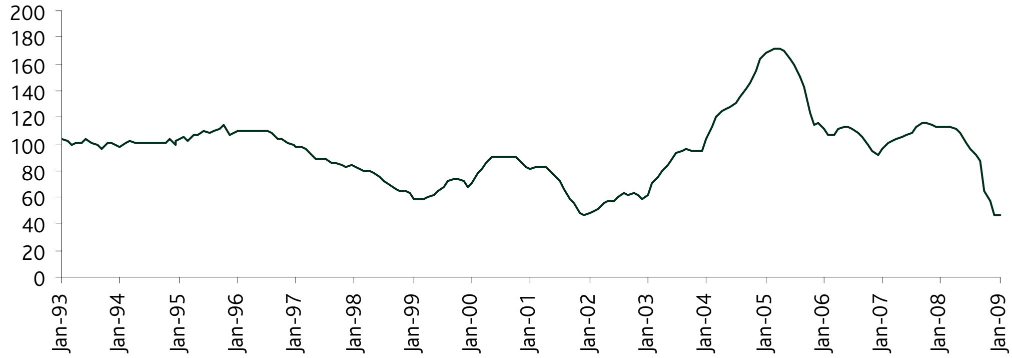
Source: Clarksons

The second-hand price index has been very strong in recent years for dry bulk carriers,. However, the index has fallen sharply in recent weeks and we expect this trend to continue given that the BDI has fallen 97% since March 2008. Again, due to a lack of transaction the index is still artificially high in our view and we would not be surprised if this were to fall to near historic lows over the coming months.

CONTAINER

The container trade is somewhat different from dry bulk as it is reliant on developed economies vs. developing economies. Containers typically transport manufactured goods and the main consumers of these products are mostly in the developed countries, hence the trade is dependent on the GDP growth of OECD economies. The key earnings indicators used are the Howe Robinson container index and Time Charter Index (rev/TEU) for container ships. Figure 14 illustrates the rev/TEU for container ships.

Figure 14: Time Charter Index (based on Rev/TEU)



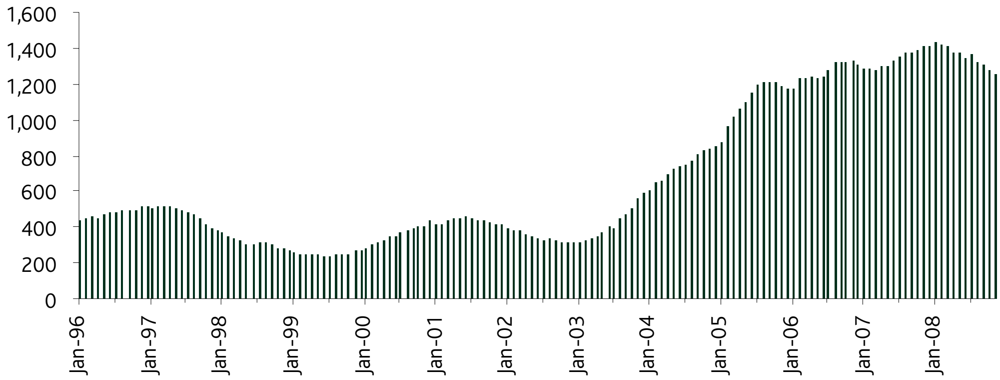
Source: Clarksons

World container trade growth has been equally strong, with the rev/TEU rising 140% from the start of 2000 to its 2005 peak. Also the Howe Robinson Index rose from 451 in January 2002 to 2093 in June 2005 - an increase of 464%. The removal of trade barriers under the World Trade Organization and the establishment of regional trade agreements have also helped the industry's growth rate. Historically the container trade has grown between 2.2x and 2.5x world economic growth. For instance, in 2007 container volumes grew 12%, which was 2.3 x global GDP growth of 5.2%. Charter rates have been on a downward trend in recent years but have dropped off sharply in recent months and are now back at 2003 levels.

Supply Side of the Container Market

The container orderbook currently stands at 55% of the fleet and capacity is expected to expand by double digits until 2011. Capacity is expected to grow 13.4% in 2008e and 12.7% in 2009e. The size of the orderbook is not surprising given that container volume growth has been particularly strong in recent times but, combined with a global slowdown, the increase in capacity could be severely detrimental to daily rates going forward.

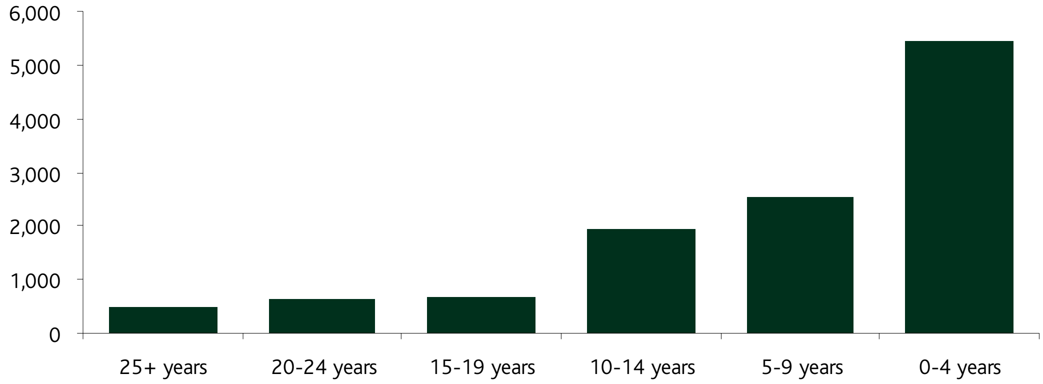
Figure 15: Container Orderbook
number of ships, unless otherwise stated



Source: Clarksons

In contrast to the dry bulk and tanker markets, the container fleet is much younger with 46% less than five years old and only 9% more than 20 years old. Consequently, the large orderbook is likely to have a material impact on the supply side.

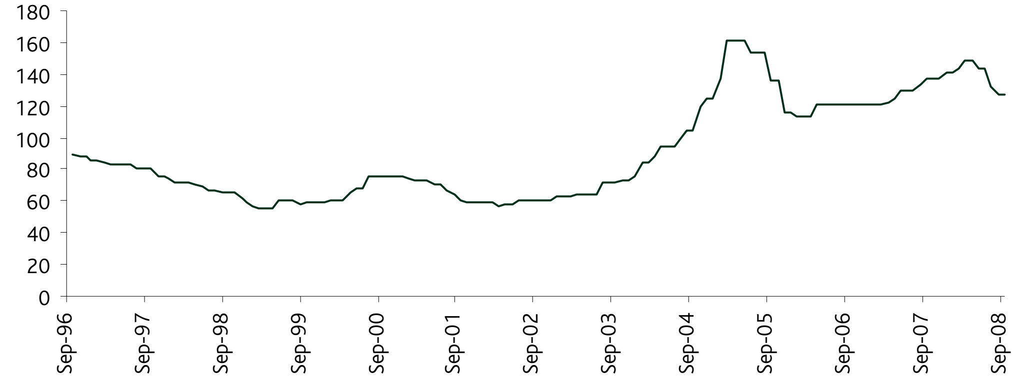
Figure 16: Container Ship Fleet Age: 46% of Fleet Less Than 5 Years Old
Number of ships, unless otherwise stated



Source: Clarksons

The second-hand price of container ships has been relatively steady in recent years. After a spike in 2005, the second-hand index has weakened. However, once current data becomes available, we suspect it will show that prices have plummeted in line with the earnings index

Figure 17: Container Ships Second Hand Prices Index: Sharp Falls Expected



Source: Clarksons

However, supply issue may not be as significant as the data suggests
While the size of the orderbook is a concern given that freight rates have fallen significantly in recent months, in practice the situation may be different. It is worth noting that some orders are likely to be cancelled as owners are refused funding or simply pull out of deals as the returns may no longer justify the investment. Also, the orderbook is somewhat exaggerated as the industry often reports new orders even when they are in the contractual stage, which means some orders will never be signed. Finally, even during the boom times, the industry's ability to deliver all the ships on time was never certain due to capacity constraints. For example, many of the new orders were given to shipbuilders with greenfield sites in China who were new entrants to the market as the traditional Korean operators were at full capacity.

However, many of these greenfield sites are ill equipped to execute the orders and the subsequent increase in raw material prices and shortage of trained labour has put further pressure on the timetable. Consequently, the supply of new ships over the next few years is likely to be more limited than the statistics would suggest.

Second-hand values not a true reflection of current value
It is worth noting that Clarkson's (the source of our second-hand value index) are stating that current values are not reflective of market condition due to the lack transactions. The second-hand indices for all fleets have held up well according to the stats, but real values are likely to be significantly lower.

SUMMARY – TANKERS TO OUTPERFORM

Overall, while demand and supply issues are a major concern for the industry, it appears that the dry and container markets are likely to bear the brunt of the downturn. The dry and container markets are exposed to growth in emerging economies and consumer spending in the West. Growth forecasts for emerging economies have been cut significantly and retail demand has plummeted in recent months, with little sign of stabilisation in either market.

Demand for oil has also weakened in the last six months with forecasts for 2009 being cut on a weekly basis. However, compared to the dry and container market, the demand for tankers is relative inelastic. In addition, the tanker orderbook is not as high, particularly given that all single hull ships need to be phased out by 2015.

II. REVENUE AND COST DRIVERS

KEY REVENUE DRIVERS

Ship owners generate revenues through leasing their ships either in the spot market or under a charter contract for a specific length of time at a fixed daily rate. Companies typically use a mixture of the two, with charters providing good revenue visibility, while the spot market often offers the opportunity to earn higher rates.

Charter contracts can be short term i.e. 1-3 years, long term (10-15 years) or very long term (25 years plus). The longer-term contracts are generally used to transport gas and are long in nature due to the heavy significant upfront investment that is required. The longer-term contracts are generally on a cost plus basis and/or inflation adjusted, where the ship owner will be paid a fixed percentage above the operating cost of the ship. This eliminates the risk of rising costs from a ship owner's perspective while securing the service of a vessel for a long period for the charterer.

The revenue line is a function of fleet utilisation x average daily rate and the example below illustrates how the revenue line would be calculated for a company that owns one vessel for a full year:

Figure 18: Revenue metrics

USD, unless otherwise stated

Stats	Example	Comment
Ownership Days	365	Number of days vessels under ownership
Available Days	340	Available days exclude days lost for repairs and maintenance (dry docking)
Operating Days	320	Actual number of days on hire generating revenues
Fleet Utilisation (%)	94%	Operating days / Available days expressed as a percentage
Average Daily Rate	10,000	Average rate earned per day from hire (determined by market)
Total Revenues	3,200,000	

Source: EFG-Hermes

KEY COST DRIVERS

Shipping companies are highly operationally geared with a high fixed cost base. The operational cost of a charter trade is shown below in figure 19. The largest segment of operating expense is crew costs, which accounts for 35% of the total cost. Repairs and maintenance costs is the next largest at c.18%.The last segment of operating cost is depreciation, which depends on the book value of the fleet.

Figure 19: Operating Expenses

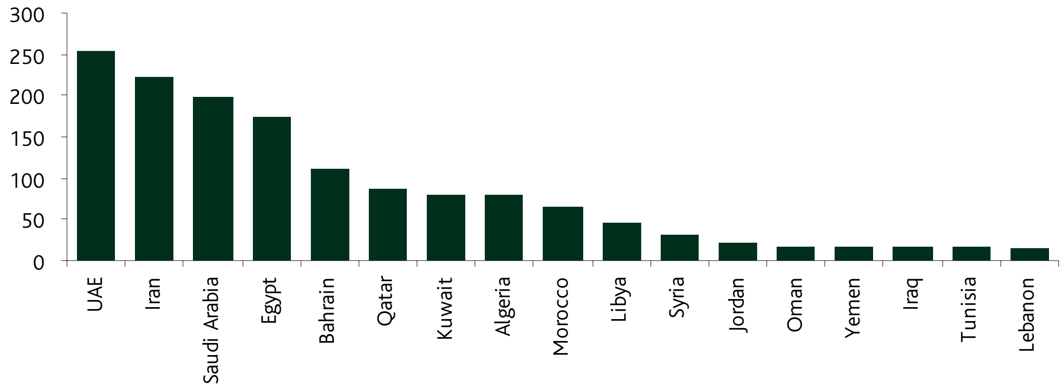
OPEX	% of Total OPEX	Comment
Crew Costs	35%	Largest operating expense. Crew costs inflation has been c.20% per annum
Insurance	12%	Cost of insuring for journey
Repairs & Maintenance	18%	Vessels are dry docked at least every 2.5 years for general servicing and maintenance.
Stores & Lubricants	10%	Required for vessel and crew
Other	5%	Miscellaneous
Depreciation	15%	A vessel's useful life spans 20-25 years, with scrap value at circa 10%. Typically depreciated in straight line form.
Total OPEX	100%	Straight line form.

In a spot trade the ship owner has an additional expense line being voyage costs. The voyage expense has averaged at around 5% total sales. For instance, using the example from figure 18, total voyage costs would amount to $160k (5% of $3.2m). Voyage costs include bunkering (fuel), port and canal charges.

III. MENA SHIPPING SECTOR

The MENA region plays an important role in the shipping world due to its position as a large natural resource producer and its geographic location along the key trade route from Asia to Europe. There are 504 ship owners in the region according to Clarksons, owning a total of 2,356 ships or 12% of the world's total fleet. The owners are a mixture of national governments such as KSA, resource producers such as Aramco, and dedicated ship owners such as Gulf Navigation. The UAE appears to have the highest number of ships but we suspect this is mainly due to company's registering their shipping subsidiary businesses in the country for admin purposes while operating outside of the UAE.

Figure 20: Total Number of Vessels Owned
Number of ships, unless otherwise stated



Source: EFG-Hermes

There are five significant ship owner operators in the MENA region, with three in Qatar, one in KSA and one in UAE. Nakilat and the NSCSA are the two large operators with sizeable vessel portfolios. Gulf Navigation is an emerging ship owner with big ambitions. Qatar Shipping and Qatar Navigation are more diversified businesses, with interests in other related and unrelated operations.

Figure 21: The Key Listed Players and Vessel Portfolios
Ownership of 50% or more, unless otherwise stated

	Share Price 01/26/09	Currency	M.Cap (mn)	M. Cap $(mn)	OIL	LNG	LPG	CHEMI-CALS	DRY BULK	CONTA-INER	TOTAL
NSCSA	17.6	SAR	5,544	1,478	17	0	0	32	0	4	53
Gulf Navigation	0.6	AED	1,208	331	3	0	0	10	0	0	13
Nakilat	14.8	QAR	8200	2,246	0	25	0	0	0	0	25
Qatar Shipping	23.6	QAR	3,971	1,087	5	0	6	0	0	0	11
Qatar Navigation	54.9	QAR	4,290	1,175	0	0	0	0	1	8	9

Source: EFG-Hermes

WE USE A FOUR-STEP INVESTMENT APPROACH TO EVALUATE THE MENA SHIPPING SECTOR:

i) Market conditions and outlook of end markets: Firstly we examine the market conditions of the key sectors that the MENA shipping companies operate in.

ii) Revenue visibility: Secondly, we break down the level and length of revenue visibility i.e. chartered vs. spot markets.

iii) Growth strategy and financing requirement of future vessels: Subsequently, in light of recent events, we focus on the funding requirement of planned CAPEX and vessel acquisitions.

iv) Valuation: Finally, we conclude with a multi-step valuation exercise to determine our recommendations

The vessel list in Figure 21 offers an insight into the exposure of the ship owners with the MENA players being mostly geared into the oil/chemical market and the gas market. Container ownership is limited to NSCSA and Qatar Navigation, which also has exposure to the dry bulk market. Below we evaluate the outlook for each of these markets.

A. MARKET CONDITIONS

Overall, we believe groups exposed to crude oil (tankers) and gas are likely to be more resilient in the current downturn. Crude oil demand is relatively inelastic and gas contracts tend to be long in nature, providing strong revenue visibility.

OIL

The seaborne oil shipping trade is dependent on the demand and supply of oil. The EU is the largest importer of oil at 28%, followed by the US at 19%. Demand for oil has weakened sharply since oil prices peaked in mid-2008, resulting in the oil price falling back nearer to USD35 per barrel – a four year low. Despite this decline, demand is expected to remain weak as global industrial output slows. Overall, Clarksons estimates suggest that US demand for oil will drop by 300k bpd in 2009 but this forecast was last updated in December 2008, and we suspect estimates may have to be cut again as demand appears to have weakened further in the last few weeks. This is also true for demand in all other countries in the table below..

Figure 22: Global Oil Demand: 2009 Estimates Still Hold Downside Risk
In BPD million, unless otherwise stated

	2004	2005	2006	2007	2008	2009e
Demand to North America						
United States	20.7	20.8	20.7	20.7	19.4	19.1
Canada	2.3	2.3	2.3	2.4	2.3	2.3
Mexico	2	2.1	2.1	2.1	2.1	2.1
Total	**25**	**25.2**	**25.1**	**25.2**	**23.8**	**23.5**
OECD Europe						
Big 4	8.3	8.2	8.2	7.9	7.8	7.7
Total OECD Europe	**15.5**	**15.6**	**15.7**	**15.3**	**15.2**	**15**
OECD Pacific						
Japan	5.3	5.3	5..2	5	4.8	4.7
Korea	2.2	2.2	2.2	2.2	2.2	2.2
Total OECD Pacific	**8.5**	**8.6**	**8.5**	**8.4**	**8.1**	**8**
Non OECD Asia						
India	2.6	2.6	2.8	3	3.1	3.2
China	6.4	6.7	7.2	7.5	7.9	8.2
Other Far East	6	6.2	6.2	6.3	6.4	6.5
Total	**15**	**15.5**	**16.2**	**16.8**	**17.4**	**17.9**
Other Non OECD						
FSU	3.8	3.9	4.1	4.1	4.2	4.3
Latin America	5	5.1	5.3	5.6	5.9	6.1
Africa	2.8	2.9	3	3.1	3.1	3.2
Middle East	5.7	6	6.2	6.5	7	7.2
Others	0.7	0.7	0.8	0.7	0.8	0.7
Global Total	**82.3**	**83.8**	**85.1**	**86.1**	**85.8**	**86.3**

Source: Clarksons

Oil Supply

In addition to healthy demand, oil production has been running at full capacity over the last few years, leading to near perfect market conditions for tankers. However, following the recent decline in the oil price it is not surprising that OPEC has cut production. This is obviously negative for the tanker market, especially given that prices have not rebounded and consequently further supply cuts are entirely possible in our view. That said, due to its inelastic nature, the demand and supply of oil is less volatile than other markets such as raw materials. Consequently, the tanker market should be more resilient than the dry or container market.

GAS – LNG AND LPG

Liquid Petroleum Gas (LPG) is the generic name given to the commercial gases propane and butane. LPG is usually derived from fossil fuel sources; manufactured during refining or extracted from oil or gas streams. LPG is mainly used for cooking, or as a fuel source for cars and domestic heating. The advantage of LPG is that it burns cleanly with no soot and is also relatively easy to transport.

Liquefied Natural Gas (LNG) is methane that has been cooled to about -163 degrees C at which point it liquefies and can be transported in tanks aboard specialized vessels. LNG is normally warmed to make natural gas and is used in heating, cooking and electricity generation. Natural gas is the cleanest burning fossil fuel. Consequently many countries are changing their mix of fossil fuel usage in favor of LNG as it will help in meeting lower emission targets.

The demand for gas has grown at a compound rate of 3% over the last six years versus 1.6% growth for oil. Going forward, the market is expected to remain healthy with recent growth sustained. Despite demand remaining relatively buoyant, there is some concern on the supply side with some LNG projects suspected to have been either delayed or shelved. LNG projects require significant capex in infrastructure and given the current financial environment it would not be entirely surprising should some projects get delayed due to financing problems. This is somewhat worrying as there are a large number of LNG carriers due for delivery in the near term, which means that rates are likely to weaken further. That said, due to the high investment costs, gas contracts tend to be long term in nature. In summary, we expect the LNG market to remain relatively resilient despite the slowdown in the economy but supply may not come on line as quickly as previously expected.

CONTAINER

Containers typically transport manufactured goods usually purchased by consumers in developed economies. Consequently the performance of containers is closely correlated to the GDP of the OECD countries. Given the current economic environment container traffic is expected to slow significantly. It appears economists are cutting GDP growth forecasts for OECD countries on a weekly basis, which suggests the container market is likely to remain weak for the foreseeable future.

DRY BULK

The dry bulk market has been particularly difficult in recent months with demand slowing for iron ore and coal. China is a key importer of raw materials and the slowdown in Asia has hit the industry hard. The closure of factories during the Olympic Games were initially thought to be temporary but the anticipated pickup in demand following the games has not materialised. This suggests that China has either built up a large inventory or is simply slowing production due to weaker demand. Either way, this is not positive for dry bulk owners and we expect the market to remain difficult in the near term at least. That said, exposure to the dry bulk market is limited to Qatar Navigation, which is expecting a vessel delivery in 2009.

CHEMICALS

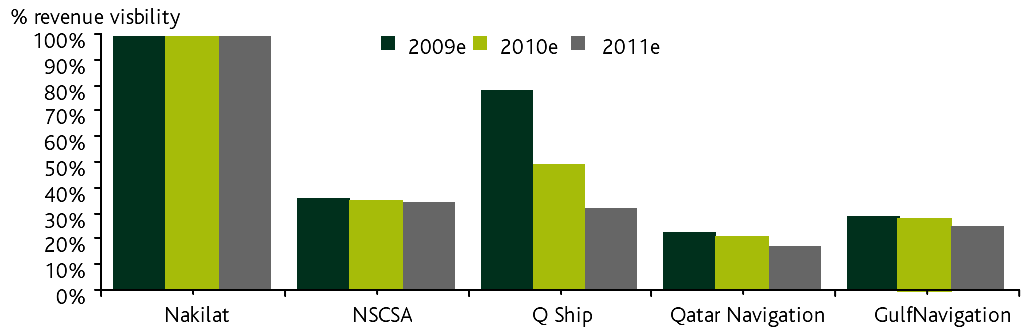
Petrochemicals, as the name suggests, are chemicals obtained from the cracking of petroleum feedstock. Petrochems are used to manufacture a wide range of products such as rubber, polyethylene plastics, anti-freeze, latex paints, textile, vinyl plastics etc. The demand for petrochems is correlated to global GDP growth, particularly emerging markets, with China and India becoming key importers of petrochems in recent years. Consequently, the market is somewhat similar to the dry (raw materials) industry. Growth in petrochems has been strong in recent years, at 5% p.a., but the outlook appears uncertain. Press stories suggest that some chemical carriers are sitting idle as spot rates have fallen below breakeven levels.

B. REVENUE VISIBILITY

Revenue visibility is an important factor when making an investment decision, but in the current climate, it has, in our opinion, become even more significant. Based on the existing contracts for each of the companies, below, we estimate the % of future revenues which are underpinned for the next three financial years.

It is worth pointing out that the revenue visibility % levels are dependent on existing charter contracts, which could be renegotiated or cancelled. In recent weeks there have been reports that some charterers have reneged on contracts signed in mid-2008, particularly in the dry market. However, many of the charterers in the MENA region are government entities or large corporates, very few are in the dry market, and according to our estimates, none were signed in the peak of mid-2008. Consequently we do not expect any cancellations.

Figure 23: Revenue Visibilty
In %, unless otherwise stated



Source: EFG-Hermes

NAKILAT

Theoretically, Nakilat's shipping revenues should be c.100% secure for the foreseeable future as it has fixed long-term contracts. However, the group's business model is reliant on the timely delivery of all its ships and of course the completion of the LNG terminals which will supply the gas. To date, Nakilat's ships have been delivered on time, however there is potential for delays to the completion of LNG terminals which would likely impact the expected ramp in revenues over the next one to two years.

NATIONAL SHIPPING COMPANY OF SAUDI ARABIA

NSCSA discloses more information regarding its contracts and thus it is easier to gauge the level of fixed revenues. For instance, the group has six oil and nine chemical tankers on charter, which make up most of the fixed contracts in our view. The remainder of the portfolio is exposed to the spot market. Overall, we estimate that 36%, 35% and 34% of our 2009e, 2010e and 2011e revenue forecasts are already locked in.

QSHIP

We believe QShip offers strong revenue visibility, especially in the near term with 78% of 2009e sales already booked. Management made a shrewd decision to charter their entire fleet during 2007 for a period of between two and five years, which means that the shipping revenues are secured at least until 2H2010e. While the charter rates have not been disclosed, we believe a fair estimate can be gauged from the recent results. Unfortunately QShip offers less disclosure on the contracts at its offshore support services (Halul) and Construction divisions. However, we have assumed revenues visibility of 70%, 50% and 30% for 2009e, 2010e and 2011e respectively.

For Halul, we know that typical contracts last three to four years, which should mean that circa 90% of 2009e revenues are underpinned, and the construction business has a solid orderbook from recent contract wins and should also have high revenue visibility. In practice, both the Halul and the Construction divisions are geared into state spending in Qatar which we expect to remain strong despite the recent drop in the oil price. As a result, QShip should continue to benefit in the near to medium term.

QATAR NAVIGATION

Qatar Navigation's revenues are more geared to shipping activity (traffic) in Qatar and are less secure by nature. That said, QN also holds a 50% stake in Halul, alongside QShip. Elsewhere in the business, it is more difficult to calculate the level of guaranteed revenues due to lack of disclosure but Qatar Nav enjoys c.90% market share of the feeder traffic from UAE to Qatar as it has exclusive contracts with QChem and Qapco and we estimate that at least 30% of these revenues are fixed. Overall, we believe 23% of 2009e, 21% of 2010e and 17% of 2011e revenues are underpinned.

GULF NAVIGATION

Gulf Navigation's revenue visibility appears somewhat limited with c.29% of 2009e, 2010e and 25% of 2011e sales fixed according to our estimates. Our view is particularly conservative as the group had five charter contracts up for renewal in the last quarter. The likelihood is that these vessels have been re-chartered, and that is what we are assuming in our forecasts, but we are reluctant to factor in any level of guaranteed income as we have no details as of now.

C. CAPEX SPEND AND FINANCING REQUIREMENTS

As a general rule of thumb, shipping is a high capex industry as vessels are expensive, not only to buy but to maintain. For example, vessels are dry docked once every 2.5 years for between 15 and 25 days and docked again for a longer period after five years for major service. Furthermore, shipping companies must acquire ships to grow market share, which can be expensive and requires financing. Invariably companies order new ships during good market conditions, i.e. when vessel prices are at their steepest. This is the current state of the market, with the orderbook at record levels. In this section, we examine the capex plans for our five companies and the level of debt we believe the group is likely to take on, and whether this debt is sustainable. For comparison purposes we have translated the numbers to USD.

Overall, we believe all the companies are in relatively good financial shape. While Nakilat appears stretched, it does have state backing and long-term charter contracts which should generate large cash inflows in future years. More importantly, Nakilat has state backing and we believe the government of Qatar will step in and offer the necessary financing should Nakilat find it difficult to raise the capital in the market. Gulf Navigation is the one stock which could struggle to raise new finances but that doesn't appear to be an issue in the short term.

Figure 24: Capex Spending
In USD million, unless otherwise stated

	2009e Capex	2009e Net Debt / EBITDA (x)
Nakilat	1,931	15.4
NSCSA	320	3.9
Q Ship	430	3.5
Qatar Navigation	99	1.3
Gulf Navigation	255	3.4

Source: EFG-Hermes

QSHIP

2009 is a significant year for Qship as it embarks on a significant capex programme. The group has a 50% share in an LPG business, which is expected to own four vessels next year. This JV is in partnership with Nakilat, which will also manage the operation. LPG vessels are relatively expensive and QShip's commitment exceeds USD500m, and we expect a significant portion of that to be paid on delivery i.e. 2009. Fortunately the group has financing already in place. In addition, the LPG tankers are on long-term charters and are a relatively low risk investment. While debt jumps to USD625m in 2009e, it looks manageable at 3.5x EBITDA, given our view that cashflows are secure. We would be more cautious should the group decide to take on more debt.

QATAR NAVIGATION

Qatar Navigation is due to take delivery of one dry bulk carrier and four container vessels in 2009. The dry bulk carrier's purchase price was USD68m and we estimate the container vessels cost c.USD20m each. Overall, we estimate 2009e capex will be USD99m. Qatar Navigation raised USD219m through a rights issue early in 2008 and consequently its net debt is relative low, peaking in 2009e at USD172m, which is at a comfortable 1.3x EBITDA. We believe Qatar Navigation is in good financial shape and could be more aggressive in its growth plans.

GULF NAVIGATION

Gulf Nav's capex peaks in 2009 as it is due to receive four more chemical vessels. Net debt also peaks in 2009e at USD255m, which stands at 3.4x EBITDA. The chemical vessels are on long-term charter and we expect the debt level to fall steadily in subsequent years. Overall, should the market stabilise, we believe Gulf Nav could be in a good position to take on additional debt for further acquisitions.

NAKILAT

As of 30 June 2008, Nakilat had outstanding capex commitments of over USD2.8bn and we estimate that circa USD2bn of that will be spent in 2009e. This is due to the fact that Nakilat is expecting delivery of most of it vessels during the year and most (c.60%) of the acquisition costs are paid in the year of delivery. We believe net debt will be stretched to USD6.7bn by Dec 2009e, which is 15.4x EBITDA but that should not be a concern at this stage as a) Nakilat is in start-up phase and b) the group is not due to make significant capital repayments until it begins generating material cash inflows. We expect the net debt to EBITDA ratio to fall steadily in the coming years, reaching 6.9x in 2011e.

NSCSA

NSCSA also has a large orderbook and it expects to take delivery of four crude tankers and 16 chemical carriers in the next few years. Capex in 2009e will reach an estimated USD320m, stretching net debt to EBITDA to 3.9x. Fortunately, NCSCA secured all financing, at attractive rates, before the recent credit crisis began to bite. As a result, the group is very comfortable with its balance sheet and is keen to acquire should good opportunities arise. That said, with the spot market close to freefall, we would be more cautious should management continue to expand in the current environment.

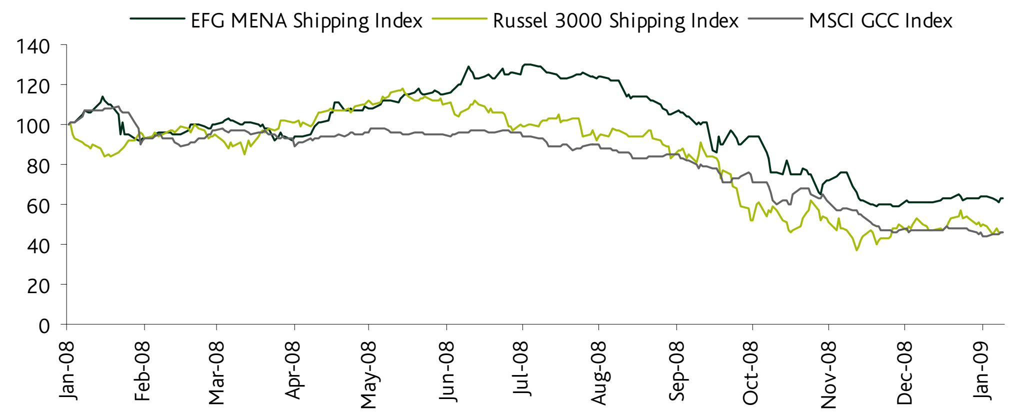
LIMITED MANAGEMENT ACCESS A RISK

As an additional risk factor, it is worth noting that EFG-Hermes has had little access to the management of the above shipping companies with the exception of National Shipping Company of Saudi Arabia and Nakilat. While we may be bearish on the short term outlook for NSCSA, we believe the group has a strong management team with a good track record. Also, Nakilat has outsourced the management of its vessels to a specialist LNG operator, Stasco (Royal Dutch Shell) and consequently there is negligible risk of a change in strategy. We have had limited contact with Qatar Shipping, Qatar Navigation and Gulf Navigation and have mainly relied on published financials and other documents as well as industry sources for our analysis.

IV. PERFORMANCE AND VALUATION

The Russell 3000 shipping index, which consists of the 20 largest US shipping companies, fell 49% in 2008 (Figure 25) and 55% since it peaked in May 2008. In comparison, the EFG MENA Shipping Index has fallen by 39% in 2008 and by 52% since it peaked in July 2008.

Figure 25: MENA Shipping Index Performance
Rebased to 100 at January 2008



Source: Bloomberg, EFG-Hermes

Overall the EFG MENA Shipping Index has outperformed the Russell 3000 Shipping index since the start of 2007 but the direction has been similar, with both dropping sharply since mid-2008.

Individually, the MENA shipping stocks have fallen in tandem, with Nakilat outperforming. While initially outperforming the broader GCC market, the stocks have underperformed the market in recent months, which reflects the bleak outlook of the industry as a whole.

Figure 26: Stock Performance
In %, unless otherwise stated

	Last Month	last 3 Months	Last 6 Months	2008
NSCSA	10%	5.2%	-47%	-40%
Gulf Nav.	-10%	-47%	-61%	-61%
Qatar Shipping	-34%	-36%	-63%	-38%
Nakilat	-33%	-43%	-58%	-28%
Qatar Navigation	-23%	-26%	-63%	-38%
GCC Index	12%	-40%	-55%	-55%

Source: EFG-Hermes, Bloomberg

VALUATION

Our preferred metrics for valuing shipping companies are Price/Book, EV/EBITDA and DCF. NAV can be useful, particularly when companies revalue their vessels to reflect the change in second-hand prices but none in our coverage have revalued in recent years. PE ratios are less effective in our view, as earnings are volatile and difficult to predict but can be useful for relative comparison purposes.

The table below illustrates the recent performance and valuation multiples of the 20 global shipping companies excluding MENA stocks.

Figure 27: Industry Comparables
In USD million, unless otherwise stated

Company	Mkt Cap	Enterprise Value	Price % Chg, 2008	P/E 2008e	P/E 2009e	PB/Share	Enterprise Value/EBITDA
A.P. Moeller-Maersk A/S	19,796	187,894	(42.7)	5.3	8.1	0.89	2.2
China COSCO Holdings Company Ltd	13,133	88,746	(75.7)	4.5	7.3	1.5	3.1
STX Pan Ocean Co Ltd.	9,676	14,927	(76.9)	1.3	2.9	4.21	11.0
MISC Berhad	8,619	37,487	(12.9)	15.4	14.9	1.56	9.4
Mitsui O.S.K. Lines, Ltd.	7,360	1,279,943	(55.3)	3.5	5.1	0.88	3.4
Nippon Yusen Kabushiki Kaisha	6,346	1,521,577	(41.6)	4.3	5.9	0.81	5.4
China Shipping Development Co., Ltd	5,317	40,252	(70.4)	6.0	8.5	1.75	6.9
China Shipping Container Lines Co Ltd	4,921	28,144	(70.7)			1.04	4.2
HYUNDAI MERCHANT MARINE Co.,Ltd	2,770	4,673,841	(11.8)	9.5	11.1		8.1
Kawasaki Kisen Kaisha, Ltd.	2,447	585,950	(65.6)	3.3	5.4	0.56	3.1
Bollore SA	2,409	3,431	(32.5)			0.56	15.2
Frontline Ltd.	2,234	34,953	(11.9)	3.0	10.2	3.25	4.7
Toll Holdings Limited	2,196	4,392	(46.8)	11.0	10.2	1.62	7.9
Frontline Ltd. (USA)	2,153	5,102	(30.0)	3.5	12.2	3.13	4.2
Tidewater Inc.	2,025	2,180	(21.0)	5.4	6.0	0.99	4.2
Mitsubishi Logistics Corporation	1,711	158,533	(28.0)	20.0	19.4	0.75	6.8
STX Pan Ocean Co., Ltd.	1,463	1,854,070	(56.6)	2.6	6.2		3.3
Bourbon SA	1,452	2,111	(51.3)	7.4	7.7	0.98	6.8
Dampskibsselskabet NORDEN A/S	1,399	4,628	(60.0)	1.6	3.7	0.82	0.8
Kirby Corporation	1,333	1,603	(41.0)	8.3	8.1	1.5	4.5
Seacor Holdings, Inc.	1,315	1,893	(24.6)	7.9	7.9	0.85	4.9
M. Cap Weighted Average		**501,507**	**(49.7)**	**5.5**	**7.4**	**1.40**	**4.8**

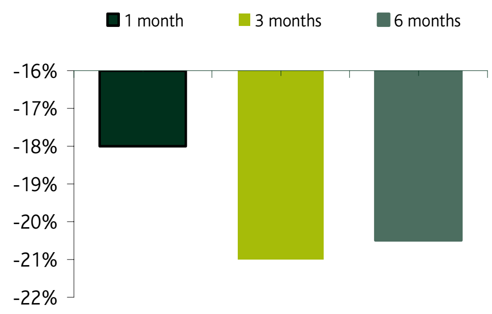
Source: Reuters, EFG-Hermes

On average the stocks have lost 50% of their value in 2008, which is broadly in line with the Russell 3000 Shipping index. As a result, the shipping sector trades on single-digit PEs for both 2008e and 2009e.

EARNINGS MOMENTUM

Forecasts for 2009 have also been pulled back significantly. As Figure 28 highlights, EPS forecast for the top five shipping companies have been cut by an average of 20% in the last six months, with the bulk of it coming in the last month. This compares to an average share price fall of c.40%, which implies that stocks have de-rated significantly and that the market is pricing in further negative news flow.

Figure 28: EPS Forecast Change in Top 5 Global Shipping Companies



Source: EFG-Hermes

The MENA shipping stocks trades at a premium on our 2009 estimates. The premium is possibly due to consensus not updating forecasts in what is a constantly moving market. However, MENA ship owners have higher exposure to the tanker market, which is more defensive and generally have stronger balance sheets and, for this reason, we would expect the stocks to trade at a small premium. The EV/EBITDA multiples are somewhat misleading as a) Nakilat is still in start-up phase and b) QShip and QNav own 30% of Nakilat, which also skews their multiples. The table below shows the adjusted EV/EBITDA multiples for QShip and QNav, stripping out the stake in Nakilat. Moreover, the MENA stocks trade at c.30% below book value (excluding Nakilat) and 50% below their global peers, which is unfair in our view.

Figure 29: Valuation Summary
In local currency, unless otherwise stated

	Currency	Mkt Cap mn	Price	Recommendation ST	LT	FV	Upside/ Downside %	2009e P/B	2009e P/E	2010e P/E	2009e EV/EBITDA	WACC %	Term Val/ Tot Val %
Qatar Navigation	QAR	4,290	54.9	Buy	Buy	82.3	50	0.48	6.6	5.6	8.6	12.8	50
Qatar Shipping	QAR	3,971	23.6	Buy	Buy	34.4	46	0.53	5.7	4.7	7.8	12.1	46
Gulf Nav.	AED	1,208	0.6	Accumulate	Neutral	0.77	38	0.55	8.5	7.0	7.1	10.8	68
Nakilat	QAR	8,200	14.8	Neutral	Accumulate	19.6	32	1.96	7.1	4.5	22.3	9.0	64
NSCSA	SAR	5,544	17.6	Sell	Neutral	14.9	-15	1.07	12.7	10.3	7.2	12.0	68
M. Cap Weighted Average (Nakilat included only in P/E)								**0.7**	**8.0**	**6.4**	**7.8**		

Source: EFG-Hermes

DCF VALUATION

Due to the uncertain outlook and volatility in the spot market, we are using aggressive assumptions in our DCF calculations, with our WACCs ranging from 9.0% to 12.8%. Further details can be found on the company sections.

Figure 30: Valuation Commentary

	2009e Revenue Visibility	Capex 2009e (USD mn)	Key Risks	Comment on Management
Qatar Navigation	23%	99	Slowdown in economic activity in Qatar	Limited contact with management
Qatar Shipping	78%	430	Slowdown in economic activity in Qatar	Company does not offer meetings with equity analyst's
Gulf Nav.	29%	255	Drop in spot and charter rates	Limited contact with management
Nakilat	99%	1,931	Delay in vessel delivery. Delay in gas plants in Qatar becoming operational.	Management of LNG vessels has been outsourced.
NSCSA	36%	320	Drop in spot and charter rates	Experienced management team with 30 year track record

Source: EFG-Hermes

KEY RECOMMENDATIONS

We are generally positive on the long-term future of the MENA shipping industry with the region well placed geographically to benefit from the increasing trade opportunities in Asia. In addition, the MENA companies have a competitive advantage through good relationships with regional resource producers. Not forgetting to mention that some receive subsidised fuel, in addition to generous financial support from local banks. However, as we continually point out in our report, the short-term outlook is difficult with the global downturn in the shipping industry potentially lasting into 2010/2011 and beyond. Our stock recommendations take many of these uncertainties into account.

Our top picks are Qatar Shipping and Qatar Navigation and we initiate with ST/ LT Buy recommendations on both stocks with price targets of QAR34.4 for QShip and QAR82.3 for QNav, implying upside of 46% and 50% respectively. Also our SOTP market cap value target for the merged entity stands at QAR9.3 billion implying 58% upside as we believe the merger will offer significant synergies.

We initiate on Nakilat with a ST Neutral LT Accumulate recommendation and a price target of QAR19.6 – implying 32% upside – as we believe the company is likely to be the most defensive shipping stock with its long-term charter contracts providing strong revenue visibility.

We initiate on Gulf Navigation with a ST Accumulate / LT Neutral recommendation with a price target of AED0.77 implying 38% upside as we suspect the group could become a consolidation target at some point in 2009.

We initiate on NSCSA with a ST Sell / LT Neutral and a SAR14.9 target implying 15% downside. The group has a significant scale and a strong management team but we suspect newsflow could get worse before getting better given the 60% exposure to the spot market and consequently we remain cautious in the near term.

QATAR SHIPPING

Short-Term Rec.: Buy	Current Price*: QAR 23.6
Long-Term Rec. : Buy	LT Fair Value : QAR 34.4

We initiate on Qatar Shipping with a ST/LT Buy recommendation and fair value of QAR34.4, implying 46% upside.

- **Qatar Shipping (QShip) is a Diversified Shipping and Construction Company**. The core shipping division operates seven vessels and the construction business, QCON, specialises in oil & gas maintenance services. QShip also owns a 50% stake in Halul, which provides vessels maintenance services for the oil and gas industry. In addition, the group has a 50% stake in an LPG JV with Nakilat and also owns 15% of Nakilat's share capital.

- **QShip is our Preferred Play on the Shipping Sector,** mostly due to the fact that it has a) little exposure to the weak spot market given its ships are on charter, and b) significant exposure to the oil and gas sector in Qatar. For example, spot rates have fallen by as much as 70% in the last few months, whereas we still expect Qatar to invest USD57bn over the next five years in oil and gas projects.

- **We Expect QShip's Revenues to Steam Ahead in 2009e by 19%** as it benefits from the continued growth from QCon and from the delivery of two new LPG vessels. Elsewhere, we are estimating flat revenues for the shipping business and a slowdown in growth at Halul. Overall, we are forecasting flat EPS growth on an underlying basis due to higher finance costs. EPS falls by 23% on an absolute basis due to 2008 being boosted by a vessel disposal.

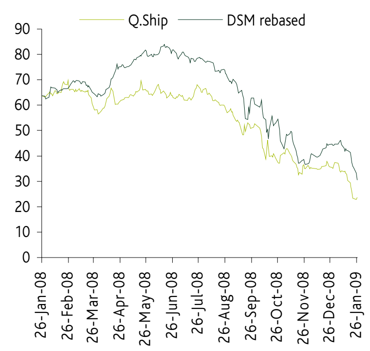
- **The Group Enjoys Strong Revenue Visibility,** with 78%, 49% and 33% of its 2009e, 2010e and 2011e sales underpinned according to our estimates. Despite the high quality of earnings the market is valuing QShip on a mere 3.0x 2009e earnings excluding the Nakilat stake, which is unfair in our view.

- **Nakilat Could Add a Further 15% to QShip's Share Price,** as we estimate that the LNG operator is trading at 32% below fair value. Currently the Nakilat stake accounts for 47% of QShip's market cap and we believe QShip's share price will remain closely correlated to the LNG transportation company.

- **We Believe There are Several Share Price Catalysts in the Near Term**. Firstly, despite the tough market conditions, we suspect risk to forecasts weighs on the upside. Also, we expect Nakilat's share price to accelerate in Q1 2009 as the group takes delivery of more of its ships. Finally, we believe QShip will be a key beneficiary of its merger with Qatar Navigation as it will ease any concerns about its debt levels.

December Year End	*2007a*	*2008e*	*2009e*	*2010e*
Revenue (mn)	*839.1*	*1,237*	*1,396*	*1,468*
EBITDA	*285.0*	*526.4*	*649.8*	*732.5*
Net Income (mn)	*610.6*	*584.2*	*451.7*	*514.0*
EPS	*6.04*	*5.31*	*4.11*	*4.67*
EPS Growth	*34.8%*	*-12.0%*	*-22.7%*	*13.8%*
DPS	*3.18*	*3.18*	*3.18*	*3.18*
PER (x)	*3.9*	*4.4*	*5.7*	*4.7*
EV/EBITDA (x)	*16.6*	*9.0*	*6.4*	*6.4*
ROE	*13.0%*	*10.3%*	*7.7%*	*8.5%*
CFPS (operating CF)	*2.95*	*3.64*	*4.27*	*4.90*
P/CF (x)	*8.0*	*6.5*	*5.5*	*4.8*
Dividend Yield	*13.5%*	*13.5%*	*13.5%*	*13.5%*
FCF Yield	*3.6%*	*-41.9%*	*19.1%*	*19.5%*
Net Debt / (Cash)	*444.5*	*744.4*	*2,261*	*2,247*

Figures in QAR million, unless otherwise stated



Estimate Changes (QAR mn)	*2007a*	*2008e Old*	*2008e New*	*2009e Old*	*2009e New*
Revenue	*839.1*	*N/A*	*1,237*	*N/A*	*1,396*
EBITDA	*285.0*	*N/A*	*526.4*	*N/A*	*649.8*
EBITDA Margin	*34.0%*	*N/A*	*42.5%*	*N/A*	*46.5%*
Net Attrib. Income	*610.6*	*N/A*	*584.2*	*N/A*	*451.7*

Stock Data	
Last Dividend	*QAR3.18 on 26 Mar 08*
Mkt. Cap / Shares (mn)	*QAR2,592 / 110*
Av. Mthly Liqd. (mn)	*QAR156*
52-Week High / Low	*QAR32.6 / 75*
Bloomberg / Reuters	*QSHS:QD / QSHP.QA*
Est. free Float	*67%*

** prices as of 26 January, 2009*

I. BACKROUND

Qatar Shipping is a diversified shipping and construction company. The core shipping division consists of seven vessels: two LPG, two Chemical and three Crude tankers. The construction arm, QCON, (The Qatar Engineering & Construction Company) specialises in oil & gas projects and plant maintenance services in Qatar. In addition, QShip owns a 50% stake in Halul, an offshore support services company that provides vessels rental and maintenance services for the oil and gas industry. Furthermore, the group has a 50% JV interest with Nakilat in four LPG vessels, and also owns 15% of Nakilat's share capital.

STRATEGY

QShip expects to benefit from the economic growth in Qatar, with a particular focus on oil and gas. The core shipping business has been somewhat de-risked through the chartering of the entire fleet. The construction division turned around after six loss-making years. Halul is exposed to the offshore drilling industry and benefits from long-term contracts. Overall, we expect infrastructure spend in Qatar to remain healthy and QShip should continue to benefit as a result.

RECENT RESULTS

QShip reported net profit numbers for 9M2008 at QAR459 million, down 4% y-o-y from QAR478 million. Excluding one-offs we estimate net income grew 38% for the nine-month period. Overall, we believe the group is on course to meet our full-year numbers.

OUTLOOK

The outlook for QShip's core businesses is mixed, with the shipping sector looking particularly weak as daily rates have plummeted in recent months. However, QShip has minimal exposure to the spot market as its vessels have been chartered for between two and five years. Elsewhere, we expect expenditure on offshore oil and gas projects to hold up in the near term, but the longer-term outlook is more dependent on a strong oil price i.e. USD50/barrel and above.

The outlook for the construction and engineering sector for Oil & Gas in Qatar remains positive as the country is on course to spend USD57 billion in the oil and gas sector over the next five years. We expect QCon to remain competitive in this market.

Q Ship's exposure to LNG is mostly through its investment in Nakilat and various JV partnerships. Please refer to the company section for our valuation on Nakilat.

RISKS

The key risk to QShip is a significant slowdown in economic activity in Qatar, particularly at the construction division which is dependent on O&G expenditure. In addition, the group is highly geared to the performance of Nakilat. Furthermore, though unlikely, the group could face a cashcall from Nakilat should it be unable to access the debt markets in 2009. Also, QShip management has a company policy not to offer one on one meeting with equity analysts and we believe this is an additional risk factor.

FORECASTS

Figure 31: Forecasts
In QAR million, unless otherwise stated

	2007a	2008e	2009e
Shipping Revenues	245	254	310
% growth		*4%*	*22%*
Offshore Support Services Revenues	226	321	358
% growth		*42%*	*11%*
Construction Services Revenues	369	662	728
% growth		*80%*	*10%*
Operating Revenue	**839**	**1,237**	**1,396**
% growth		*47%*	*13%*
Shipping Profits	138	125	144
Margin	57%	49%	46%
Offshore Support Services Profits	79	159	170
Margin	35%	50%	47%
Construction Services Profits	71	107	117
Margin	19%	16%	16%
PBT	**288**	**389**	**433**
Margin	34%	32%	30%

Source: EFG-Hermes

REVENUES

We forecast shipping revenues to remain relatively flat in 2008e before rising 22% in 2009e as the group benefits from the delivery of two additional LPG vessels. Both the construction and offshore services divisions are expected to deliver impressive top-line growth in 2008e after strong contract wins during the course of last year. Going forward, we have little information on the total orderbook or length of contracts but we anticipate further growth albeit at a much slower pace.

MARGINS

We forecast margin contraction of 200 bps in 2008e and a further 200bps in 2009e. QCon has reported lower margins in 1H 2008 and we suspect the new contract wins are slightly less profitable than the existing orderbook. In addition, we suspect the LPG division is also less profitable than the rest of the fleet.

II. VALUATION

Figure 32: DCF of Core Business
In QAR million, unless otherwise stated

	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	**526**	**650**	**733**	**753**	**734**	**617**	**635**	**654**	**674**	**701**
Change in Working Cap	68	11	5	4	(2)	(18)	0	0	0	(1)
Capex	(568)	(1,556)	(44)	(46)	(45)	(77)	(79)	(82)	(84)	(87)
FCF	**26**	**(895)**	**694**	**711**	**687**	**522**	**555**	**572**	**589**	**614**
Discount Factor	1.00	0.89	0.80	0.71	0.63	0.57	0.50	0.45	0.40	0.36
Discounted FCF	26	(798)	552	505	331	314	288	265	246	226
Perpetual Growth	3.0%									
WACC	12.1%									
PV of Cash Flows 2008-17e	1,956									
Terminal Value	**2,489**									
Total Value	4,445									
No. of Shares (mn)	110									
LTFV per Share (QAR)	**40.4**									

Source: EFG-Hermes

We use a SOTP valuation for QShip, with the core business (including Halul) valued through DCF. Please note, we have deducted net debt in our sum of the parts calculation (below).

Our key assumptions are as follows:

1. Total WACC 12.1%
2. Terminal growth rate 3.0%

Figure 33: Sensitivity Table
In QAR, unless otherwise stated

Terminal Growth	WACC: 10.0%	11.0%	12.1%	13.0%	14.0%
2.0%	50	44	38	34	31
2.5%	53	45	39	35	31
3.0%	55	47	**40**	36	32
3.5%	58	49	42	**37**	33
4.0%	61	51	43	38	34

Source: EFG-Hermes

SOTP

Figure 34: SOTP
In QAR million, unless otherwise stated

	Value	Per share (QAR)	Comment
DCF Value for Core Business	4,445	40.4	DCF
15% Nakilat	1,229	11.2	Current market price
Associates	372	3.4	5x 2008 Operating profit
Less Net Debt 2009E	(2,261)	(20.6)	2009e
SOTP	**4,948**	**34.4**	
Current Share Price (QAR)		23.6	
% Upside		**46**	

Source: EFG-Hermes

INITIATE WITH ST BUY / LT BUY

Our SOTP valuation implies a fair value of QAR34.4, which suggests an upside potential of 46%. However, the Nakilat stake is worth 47% of QShip's market cap, which means the market is valuing QShip’s core business on 3.0x earnings. This is harsh in our view given the quality of earnings at QShip.

Also, it is worth noting that our capex assumptions are particularly aggressive and the planned outlay could be spread over a longer period of time than we are currently forecasting. This would reduce our estimated debt and interest payments in the short term. Furthermore, the bulk of the capital expenditure is assigned for the LPG JV, which has its revenues underpinned. As a result, we are not overly concerned about the group's debt levels.

QShip's valuation is highly geared into the performance of Nakilat, which is currently undervalued in our view. Our fair value stands at QAR19.6 vs. the current price of QAR14.8. This could add a further QAR3.6 to our QShip fair value – an increase of 15%.

In summary, QShip’s core shipping business appears de-risked in the short term through charter contracts. Construction and offshore support services should continue to benefit from states spending, which is expected to remain strong. Furthermore, the stake in Nakilat could add QAR3.6 to the existing share price. Finally, we believe QShip will benefit from the merger between itself and Qatar Navigation, which should ease any concerns about debt. With the above in mind, we initiate with a ST / LT BUY recommendation and a QAR34.4 price target.

III. FINANCIAL FORECASTS

Income Statement (December Year End)

In QAR million, unless otherwise stated

	2007	2008e	2009e	2010e	2011e
Revenue	**839**	**1,237**	**1,396**	**1,468**	**1,528**
Change	95%	47%	13%	5%	4%
COGS (excluding Depreciation)	(497)	(814)	(968)	(1,010)	(1,047)
As % ofSales	59%	66%	69%	69%	69%
Gross Profit	**342**	**424**	**428**	**457**	**480**
Gross Profit Margin	39%	48%	43%	43%	42%
SG and A	(83)	(85)	(88)	(91)	(94)
As % of Sales	10%	7%	6%	6%	6%
EBITDA	**285**	**526**	**650**	**733**	**753**
EBITDA Margin	34%	43%	47%	50%	49%
Depreciation	57	64	70	73	76
Net Operating Profit	228	463	580	659	677
Net Interest Expense	(54)	(72)	(150)	(203)	(205)
Non-Operating Income	333	197	22	58	32
Net Profit	**611**	**584**	**452**	**514**	**504**
EPS (QAR)	**6.0**	**5.3**	**4.1**	**4.7**	**4.6**

Source: Qatar Shipping, EFG-Hermes estimates

Balance Sheet Statement (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Cash & Liquid Assets	**396**	**573**	**5**	**210**	**84**
Accounts Receivable	267	396	447	470	489
Net Accounts Receivable	267	396	447	470	489
Inventory	5	12	14	15	15
Total Current Assets	**668**	**982**	**465**	**695**	**588**
Net Plant	1,496	2,000	3,486	3,457	3,426
Contract Work in Progress	0	46	46	46	46
Loans to LNG companies	459	478	478	478	478
Net Investments	2,942	3,630	3,486	3,806	3,898
Other Fixed Assets	114	181	248	315	382
Total Assets	**5,679**	**7,365**	**8,578**	**8,962**	**8,988**
Accounts Payable	269	495	558	587	611
Total Payables	269	495	558	587	611
Current Portion of Short term loan	97	59	70	66	63
Total Current Liabilities	**365**	**554**	**628**	**654**	**674**
Loans	**582**	**1,136**	**2,073**	**2,268**	**2,119**
Total Provisions	17	20	20	20	20
Total Liabilities & Provisions	**964**	**1,710**	**2,721**	**2,941**	**2,813**
Shareholder's Equity	**4,715**	**5,655**	**5,857**	**6,021**	**6,175**
Total Liabilities & Equity	**5,679**	**7,365**	**8,578**	**8,962**	**8,988**

Source: Qatar Shipping, EFG-Hermes estimates

Cash Flow Statement (December Year (End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Net Operating Profit	**342**	**463**	**580**	**659**	**677**
Depreciation & Amortisation	57	64	70	73	76
Other Operating Inflows (Outflows)	(347)	(182)	(41)	(43)	(23)
Net Cash Flow from Operating Activities	**53**	**344**	**609**	**690**	**730**
Cash Flow from Investing	**(48)**	**(383)**	**(1,486)**	**28**	**28**
Net Cash from Op. and Investing Activities	5	(39)	(877)	717	757
Net Movement in Loans	(50)	621	948	191	(152)
Net Cash Flow from Financing	**(746)**	**198**	**448**	**(362)**	**(707)**
Change in Cash	**(468)**	**216**	**(569)**	**206**	**(127)**

Source: Qatar Shipping, EFG-Hermes estimates

QATAR NAVIGATION

29 JANUARY 2009

QATAR | SHIPPING

Short-Term Rec.: Buy	Current Price*: QAR 54.9
Long-Term Rec. : Buy	LT Fair Value : QAR 82.3

We initiate on Qatar Navigation with a ST/LT Buy recommendation and a price target of QAR82.3, implying 50% upside.

- **Qatar Navigation is a Diversified Shipping and Transportation Company.** In addition, the group owns 50% of Halul, an offshore support services business, 15% of the share capital of Nakilat – an LNG vessel operator, and 15% of Qatar Shipping.

- **Qatar Nav. is A Play on the Qatari Economy, which is a Positive Given the Country's Solid Fundamentals.** We expect the government to continue with its substantial expansion plans and Qatar Nav. should be one of the key beneficiaries. Longer term, we believe some of Qatar Nav's non-core assets can be sold or divested which could add further value.

- **Nakilat Stake Offers Upside Potential.** We believe QNav's stake in Nakilat is undervalued and could potentially add 12% to the current share price. Our fair value for Nakilat is QAR19.6 vs. the current price of QAR14.8. In addition to exposure to a high-growth economy, Qatar Navigation has little debt which is reassuring in the current environment.

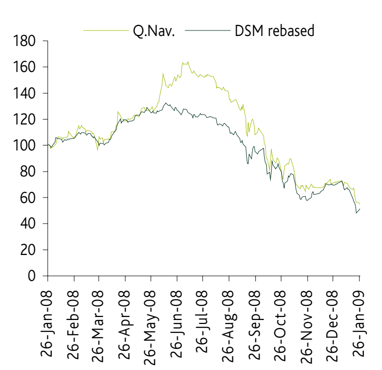
- **We Expect the Group to Deliver Another Solid Performance in 2009**, primarily driven by the Marine Transportation division as it takes delivery of four new container vessels and one dry bulk carrier. Elsewhere, we expect the Dubai operation to weaken and marine services to remain steady.

- **The Group is Exposed to a Potential Slowdown in Economic Activity in Qatar** as it has few long-term fixed contracts but we expect the Qatari economy to be the most resilient within the GCC. Furthermore, while unlikely in our view, the group could face a cash call from Nakilat if it cannot access the debt markets in 2009.

- **Qatar Navigation Offers Compelling Value** as it is trading on 6.6x 2009e (3.3x ex-Nakilat) P/E, and the recent weakness in the share price should be used as a buying opportunity. The group offers exposure to the Qatar economy, which should remain relatively resilient due to significant government investment. In addition, it owns assets that are undervalued, which could offer material upside in the medium term. Furthermore, we are positive on the recently announced potential merger with QShip as we believe such a deal makes sense and could unlock further shareholder value.

December Year End	*2007a*	*2008e*	*2009e*	*2010e*
Revenue (mn)	*1,041*	*1,213*	*1,416*	*1,638*
EBITDA	*297.8*	*390.5*	*461.3*	*542.4*
Net Income (mn)	*437.9*	*546.3*	*497.5*	*589.4*
EPS	*9.36*	*9.11*	*8.29*	*9.82*
EPS Growth	*77.9%*	*-2.7%*	*-8.9%*	*18.5%*
DPS	*5.0*	*3.9*	*3.9*	*3.9*
PER (x)	*5.9*	*6.0*	*6.6*	*5.6*
EV/EBITDA (x)	*18.7*	*14.2*	*12.1*	*7.6*
ROE	*7.2%*	*6.5%*	*5.8%*	*6.6%*
CFPS (operating CF)	*4.10*	*3.02*	*6.08*	*7.34*
P/CF (x)	*13.4*	*13.4*	*18.2*	*9.0*
Dividend Yield	*9.1%*	*7.1%*	*7.1%*	*7.1%*
FCF Yield	*2.7%*	*1.8%*	*4.2%*	*15.4%*
Net Debt / (Cash)	*1,200*	*580.4*	*578.9*	*(31.1)*

Figures in QAR, unless otherwise stated



Estimate Changes	*2007a*	*2008e*		*2009e*	
(QAR mn)		*Old*	*New*	*Old*	*New*
Revenue	*1,041*	*N/A*	*1,213*	*N/A*	*1,416*
EBITDA	*297.8*	*N/A*	*390.5*	*N/A*	*461.3*
EBITDA Margin	*28.6%*	*N/A*	*32.2%*	*N/A*	*32.6%*
Net Attrib. Income	*437.9*	*N/A*	*546.3*	*N/A*	*497.5*

Stock Data	
Last Dividend	*QAR5.0 on 25 Feb 08*
Mkt.Cap /shares (mn)	*QAR3,294 / 60*
Av. Mthly Liqd. (mn)	*QAR235*
52-Week High / Low	*QAR164 / 64.7*
Bloomberg / Reuters	*QNNS:QD / QNNC.QA*
Est. free Float	*100%*

** prices as of 26 January, 2009*

I. BACKROUND

Qatar Navigation is a diversified shipping and transportation company. The group's interests include a shipping agency, cargo handling, marine transportation, freight services, marine services, ship repair among others. In addition, the group has a 50% stake in Halul, an offshore support services business, owns 15% of the share capital of Nakilat, the LNG gas transportation company, and 15% of Qatar Shipping.

The key divisions are the Shipping Agency (27% of sales), Marine Transportation (18% of sales), and Commercial Activities (11% of sales). The agency business represents bulk of the ship owners in Qatar and has material market share of the cargo handling operation at Doha port. The Marine Transportation division currently operates four container vessels but is expected to take delivery of four additional containers and one dry carrier in 2009. The Commercial division is involved in Marine Services to the Qatar fishing industry. Going forward, we expect Marine Transportation to become the largest division with 30% of sales in 2009e.

STRATEGY

Qatar Navigation's mission statement is to provide world class shipping and transportation services, but the overall strategy is somewhat unclear. The group operates a series of businesses closely related to shipping and transportation, and historically management has invested in areas perceived to have growth potential. For example, the decision to expand the container business was made at a time when the shipping market was buoyant. While this has worked to date, we believe the group will need to be more focussed in future.

RECENT RESULTS

Qatar reported 9M net profit growth of 40% Y-o-Y, from QAR345.1 million to QAR487.9 million for the period to September 2008. We believe growth was primarily driven by the Commercial and Marine Transportation divisions, which suggests that traffic into Qatar did not slow during the quarter. With 90% of our 2008e forecast already achieved, we expect the group to comfortably meet our FY forecasts.

FORECAST

Figure 35: Forecasts
In QAR million, unless otherwise stated

	2008e	2009e	2010e
Dubai Operations	114	108	103
Commercial Activities	290	310	313
Shipping Agencies	235	243	243
Marine Transportation	211	365	553
Navigation Freight Services	48	49	51
Shiprepair & Fabrication	33	38	44
Offshore Services	9	0	0
Halul	274	302	332
Total Revenues	**1,214**	**1,416**	**1,638**
Dubai Operations	21	23	21
Commercial Activities	47	52	52
Shipping Agencies	110	118	118
Marine Transportation	75	131	197
Navigation Freight Services	23	24	25
Shiprepair & Fabrication	12	14	16
Offshore Services	3	0	0
Halul	123	128	145
Total Operating Profit	**415**	**490**	**575**

Source: EFG-Hermes

Going forward we expect the Marine Transportation division to be the key growth driver as the group expands its cargo capacity by 75% and adds a dry carrier to its fleet. While we are cautious on the container market, we believe QN's business will be more resilient as it is dependent on the UAE to Doha traffic, which should hold up relative to other routes. Elsewhere, we expect the Dubai operation to lose market share due to increased competition and Shipping Agency division to remain steady.

Overall, we are forecasting a margin contraction of 235 basis points in 2009e due to weak market conditions. However, we expect profitability to improve in 2010e by 140bps as the market begins to recover.

RISKS

The key risks to Qatar Navigation are: a) economic slowdown in Qatar b) underperformance at Nakilat c) potential cash call from Nakilat if it cannot raise cash through the debt markets. The group is also exposed to the property sector in Qatar which has started to weaken, but this only accounts for 5% of our SOTP value. Further, QN has minimal levels of debt with interest cover at a comfortable 10x for 2008e. Also, it is worth noting that we have had limited contact with the management team.

II. VALUATION

Qatar Nav is a mini transportation conglomerate and we use a combination of DCF and SOTP to determine fair value.

Figure 36: DCF of Core Business
In QAR million, unless otherwise stated

	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	**475**	**560**	**657**	**699**	**765**	**619**	**638**	**644**	**644**	**644**
Change in Working Cap	(37)	(39)	(42)	(16)	(30)	(49)	(1)	0	0	0
Capex	(268)	(357)	(164)	(172)	(188)	(145)	(149)	(151)	(151)	(151)
FCF	**170**	**165**	**451**	**511**	**548**	**425**	**488**	**493**	**493**	**493**
Discount Factor	1.00	0.89	0.79	0.70	0.62	0.55	0.49	0.43	0.38	0.34
Discounted FCF	170	147	354	356	262	267	239	212	188	203
Perpetual Growth	3.0%									
WACC	12.8%									
PV of Cash Flows 2008-17e	2,398									
Terminal Value	**2,064**									
Total Firm Value	4,462									
Estimated Net (Debt) / Cash	580									
Total Equity Value	3,941									
No. of Shares (mn)	60									
LTFV per Share (QAR)	**65.7**									

Source: EFG-Hermes

Figure 37: SOTP
In QAR million, unless otherwise stated

	Total Equity Value	Per share (QAR)	Comments
DCF Core Business	3,944	65.7	DCF
Nakilat Stake	1,230	20	At market price
QShip Stake	389	6	At market price
Arab Chemical Carriers	181	3	At Cost
Property	431	7	
Total	**6,175**	**103**	
Conglomerate Discount (20%)	(1,235)	(20.7)	
SOTP	**4,940**	**82.3**	
Current Share Price (QAR)		54.9	
Upside (%)		**50%**	

Source: EFG-Hermes

We have valued the core business on a DCF basis, Nakilat and QShip at current market value and everything else at cost. Our fair value for Nakilat stands at QAR19.6 versus the current share price of QAR14.8, and this could add QAR6.5 to our current fair value – implying further upside of 12%. We have applied a 20% conglomerate discount to our total value to account for potential modelling error. Despite this, our SOTP implies a fair value QAR82.3 vs. the current price of QAR54.9. suggesting a potential upside of 50%.

INITIATE WITH ST / LT BUY RECOMMENDATION

Overall, we remain positive on the near-term prospects for Qatar Navigation as we expect the economy in Qatar to be relatively resilient. In addition, the group's non-core assets are undervalued in our view and could offer significant upside potential in the medium term. With this in mind, we initiate with a ST/LT Buy recommendation.

III. FINANCIAL FORECASTS

Income Statement (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Revenue	**1,041**	**1,213**	**1,416**	**1,638**	**1,721**
Change	4%	17%	17%	16%	5%
COGS (excluding Depreciation)	(678)	(738)	(855)	(981)	(1,030)
As % Sales	*65%*	*61%*	*60%*	*60%*	*60%*
Gross Profit	**363**	**475**	**560**	**657**	**691**
Gross Profit Margin	35%	39%	40%	40%	40%
SG and A	(65)	(85)	(99)	(115)	(121)
As % Sales	*6%*	*7%*	*7%*	*7%*	*7%*
EBITDA	**298**	**391**	**461**	**542**	**571**
EBITDA Margin	29%	32%	33%	33%	33%
Depreciation	60	61	71	82	86
Net Operating Profit	238	330	391	460	484
Net Interest Expense	(59)	(46)	(42)	(38)	(34)
Non-Operating Income	375	376	266	287	324
Net Profit	**554**	**660**	**614**	**709**	**775**
EPS (QAR)	**9.4**	**9.1**	**8.3**	**9.8**	**10.9**

Source: Qatar Nav, EFG-Hermes estimates

Balance Sheet Statement (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Cash & Liquid Assets	**281**	**72**	**36**	**180**	**403**
Accounts Receivable	227	267	311	360	379
Net Accounts Receivable	227	267	311	360	379
Inventory	96	109	127	147	155
Prepaid Expenses	152	148	148	148	148
Total Current Assets	**756**	**597**	**623**	**836**	**1,084**
Net Plant	882	1,079	1,364	1,446	1,532
Net Investments	93	91	91	91	91
Available for Sale securities	6,024	7,450	7,460	7,474	7,491
Other Fixed Assets	45	75	98	122	148
Total Assets	**7,800**	**9,291**	**9,637**	**9,969**	**10,347**
Accounts Payable	130	146	170	197	207
Other Payables	165	174	174	174	174
Total Payables	295	319	344	370	380
Current Portion of Short term loan	1,087	209	66	66	66
Total Current Liabilities	**1,382**	**528**	**410**	**437**	**447**
Loans	**300**	**366**	**566**	**516**	**466**
Total Provisions	43	32	32	32	32
Total Liabilities & Provisions	**1,725**	**926**	**1,008**	**985**	**945**
Shareholder's Equity	**6,074**	**8,365**	**8,629**	**8,984**	**9,402**
Total Equity & Liabilities	**7,800**	**9,291**	**9,637**	**9,969**	**10,347**

Source: Qatar Nav, EFG-Hermes estimates

Cash Flow Statement (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Profit for the Year	**438**	**546**	**497**	**589**	**651**
Depreciation & Amortisation	60	61	71	82	86
Other Operating Inflows (Outflows)	(193)	(380)	(161)	(193)	(209)
Net Cash Flow from Operating Activities	**305**	**227**	**407**	**479**	**528**
Cash Flow from Investing	**(743)**	**(120)**	**(225)**	**(13)**	**12**
Net Cash from Op. and Investing Activities	(438)	108	182	466	541
Net Movement in Loans	573	(813)	(280)	(66)	(66)
Net Cash Flow from Financing	**339**	**(254)**	**(80)**	**133**	**133**
Change in Cash	**(158)**	**(192)**	**59**	**560**	**640**

Source: Qatar Nav, EFG-Hermes estimates

KINDLY REFER TO THE
IMPORTANT DISCLOSURES AND
DISCLAIMERS ON BACK PAGE

APPENDIX A QNAV AND QSHIP MERGER

On the 24 November 2008, the Qatari government asked the management of QShip and Qatar Navigation to evaluate the possibility of a merger with a view to improve profitability.

We believe a merger between Qatar Navigation and Qatar Shipping would create a sizeable company with enough scale to weather the current downturn. At current market prices, the Newco will have a market cap of QAR5.9bn, and generate revenues of c.QAR3bn and net income of QAR1BN in 2009e, making it the 9th largest company on the Doha Stock Exchange by market cap. However, our SOTP value, assuming 5% cost synergies, suggests a fair value of QAR9.3bn, implying upside of 58%. In addition, we believe asset disposals could add further value for shareholders and consequently we initiate with a ST/LT Buy rating on both stocks

BACKGROUND

We believe combining the two Qatari companies makes sense in more ways than one. For instance, both are of similar size from a market cap and profitability perspective. Both are primarily exposed to the Qatar economy and management know each other well through various joint ventures and cross ownership of other companies.

Figure 38: Key Shareholders

	Qatar Navigation	% OWNERSHIP
Public		100%
Foreign Ownership Limits		
Open to GCC Investors		25%
Open to Foreign Investors		25%

	Qatar Shipping	% OWNERSHIP
Qatar Petroleum	Government	18%
Qatar Navigation	Corporate	15%
Public		67%
Foreign Ownership Limits		
Open to GCC Investors		25%
Open to Foreign Investors		25%

Source: EFG-Hermes

The shareholder list of Qatar Navigation is not published. The only details available are that foreign ownership limit stands at 25% and no one person can hold more than 5% of the shares. More information is available for QShip, with QNav and Qatar Petroleum owning 15% and 18% respectively.

BUSINESS MODELS

QShip has a more focussed streamlined business model, with long-term contracts and consequently higher quality earnings. In contrast, Qatar Navigation is a mini conglomerate with a more diversified business that is highly geared to shipping and related services activity within the GCC, in particular Qatar.

However, the key differentiator is the level of financial gearing. Qatar Navigation has relatively little debt, whereas QShip is highly geared, (or will be after paying for the LPG vessels). By merging, QN will have access to a more stable business that will allow it to weather the downturn more comfortably. In return it will have to share the burden of QShip's debt.

From Q Ship's perspective, the group will be more exposed to the regional economy but will have access to a company generating c.QAR500m of free cashflow from 2010e onwards, providing financial support should the market continue to deteriorate.

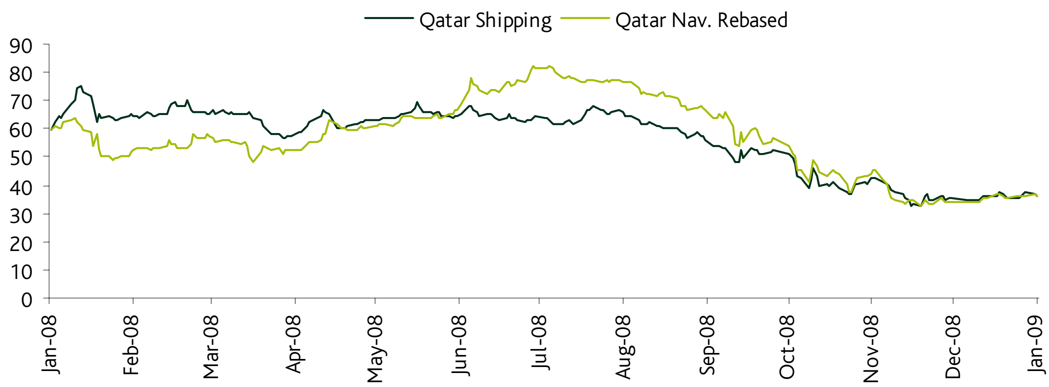
Figure 39: Combined P&L
In QAR million, unless otherwise stated

	2009e QNav.	2009e Qship	2009e Combined
Revenue	**1,416**	**1,396**	**2,812**
EBITDA	**409**	**650**	**1,059**
EBITDA Margin	29%	47%	**38%**
Depreciation	71	70	**141**
Net Operating Profit	391	580	**971**
Net Interest Expense	(30)	(150)	**(180)**
Non-Operating Income	213	31	**244**
Net Profit	**626**	**461**	**1,088**
Net Debt	**317**	**2,261**	**2,578**

Source: EFG-Hermes

The one-year share price performance shows that QN is the more volatile stock, with the shares performing more in line with the shipping industry. Qatar Nav's stock outperformed in Q2 as the shipping indices hit record highs but has come off significantly since. In contrast, QShip has been relatively stable throughout the year, only weakening in line with the overall market.

Figure 40: Relative Performance



Source: Bloomberg

QAR3 BILLION REVENUE COMPANY

The two groups combined will generate revenues of almost QAR3bn in 2009e and net income of just over QAR1bn according to our estimates, before any synergies.

SYNERGIES

We believe the merger was initiated with a view to obtain cost synergies. The obvious area to cut costs would be general admin costs, which amount to c.QAR100m in total. However, we suspect many of Qatar Navigation's ancillary services make an insignificant contribution to the bottom line, and or, are loss making. Subsequently, the potential for cost cutting could be substantial should management decide to be aggressive in their attempts improve profitability.

Figure 41: Synergies

% Cost Savings	Change in NI	% Change in NI
1%	20.3	2%
2%	40.6	4%
3%	60.9	6%
4%	81.2	8%
5%	101.5	10%

Source: EFG-Hermes

The total absolute cost base according to our estimates will be c.QAR2bn in 2009. We calculate that a 1% reduction in costs will improve NI by 2%. Overall we estimate that 5% cost synergies are obtainable.

MERGER OF EQUALS?

Unfortunately, no details regarding the merger structure have been published and it is difficult to ascertain the likely share split. Below we illustrate the potential difference in the share split if it were to be calculated on historical share price performance.

Figure 42: Merger
In QAR million, unless otherwise stated

	QShip Market Cap	QNav Market Cap	Total	QShip Weighting	QNav Weighting
Current	2,590	3,290	5,880	44%	56%
3 Month average	4,943	5,829	10,772	46%	54%
6 Month average	6,000	7,399	13,399	45%	55%

Source: EFG-Hermes

The current price suggests the market expects a c.55:45 split as in favour of Qatar Navigation. However, six months ago Qatar Nav was larger by almost 25%. On balance, we believe a 55:45 split will be the most likely case but arguably Qatar Navigation deserves a larger share of the pie as it has been the bigger of the two more recently. With this in mind, if it is not a 55:45 split, then we suspect Qatar Nav would be the more likely to be the larger shareholder. Consequently, we believe the best way to buy shares in the newco would be through Qatar Navigation.

VALUE CREATION

Aside from cost savings, we believe there are significant opportunities to create value. For instance, assuming better market conditions, we believe the market is likely to attach a higher value to Halul if it were divested or purchased by a trade buyer. Halul is an offshore support services business that services the oil and gas industry. Revenues are usually underpinned with contracts lasting two to four years. Furthermore, we believe companies similar to Halul trade on the market at circa 7x earnings. Moreover, further value can be added selling the smaller JV operations to create a more focussed company.

NAKILAT STAKE

The obvious value creation potential is through the stake in Nakilat , which stands at 30% of the newco. At the current price, the Nakilat stake accounts for 42% of the combined groups market cap. Our fair value for the LNG operator stands at QAR19.6 vs. a current price of QAR14.8 – implying that it could add a further QAR780m to the total value of the newco (8% of current fair value).

FAIR VALUE

Our SOTP value for the newco stands at QAR9.3bn, implying a potential upside of 58%. This assumes a fair value of QAR4.5bn for Qatar Navigation and QAR3.8bn for QShip. In addition, we are assuming the cost savings of QAR100m is worth QAR1,000m (discounted at 10% into perpetuity).

CONCLUSION

The merger creates a sizeable shipping company, with enough scale to withstand these tough conditions. Beyond the current cycle, we believe the group will now be in a strong position to consolidate the market as and when conditions do improve. However, in order to acquire, we suspect management will need to dispose of some non-core assets and become a focussed shipping and related services operator.

QATAR GAS TRANSPORT, NAKILAT

29 JANUARY 2009

QATAR | SHIPPING

Short-Term Rec.: Neutral	Current Price*: QAR 14.8
Long-Term Rec. : Accumulate	LT Fair Value : QAR 19.6

We initiate on Nakilat with a ST Neutral / LT Accumulate rating and a LT fair value of QAR19.6, implying 32% upside.

- **Qatar Gas & Transport Company, Aso Known as 'Nakilat', was Established in 2004 to Build a Large Fleet of Vessels to Transport LNG Produced in Qatar.** Qatar has the third-largest gas reserves in the world and is expected to become the largest global exporter of LNG by 2011. The long-term demand for natural gas is expected to remain healthy as it is the cleanest burning fossil fuel. To facilitate the transportation of natural gas, the LNG plants have awarded Nakilat 25-year charter contracts to secure the supply of the LNG vessels. In total, Nakilat is expected to own 54 LNG vessels by 2010. In addition to natural gas, the group aims to diversify into shipyard repair, LPG and sulphur vessels.

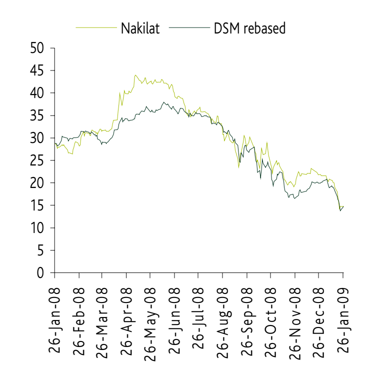
- **We Expect Nakilat to be Fully Operational by 2011** as it takes delivery of 18 vessels in 2009 and a further four in 2010. We estimate the daily rate for the LNG vessels to be between USD80k and USD110k, and cost per day at approximately USD15k. This results in a 2011e EBITDA of QAR3.2 billion and EPS of QAR3.5, leaving the shares trading on a lowly 4.3x 2011e earnings. In addition, we expect the group to employ an 80% dividend payout ratio, which offers an impressive 18.5% yield on our 2011e.

- **Nakilat's Business Model Appears Robust and Defensive** given the nature of its contracts. However, the business is exposed to execution risk, especially in the short term. For instance, the group is reliant on the timely delivery of its ships and, while this has not been a problem to date; the risk of delay to future projects is entirely possible. In addition, due to the lack of disclosure, we do not know the consequences for Nakilat if the LNG projects are delayed. Finally, the group will need to raise another USD1bn in 2009e, which may be more difficult in the current environment but we suspect the government of Qatar will step in and offer financing if necessary.

- **We are Positive on Nakilat's Future Prospects and we Believe the Stock Offers Solid Defensive Characteristics**, particularly with its generous payout ratio. Our DCF valuation suggests a fair value of QAR19.6, implying 32% upside. However, we are likely to be more bullish in our recommendation once the LNG projects are confirmed as completed, when more vessels are delivered, and when we have additional information on the revenue/cost dynamics of the larger ships, which will give us more confidence in our forecasts.

December Year End	*2007a*	*2008e*	*2009e*	*2010e*
Revenue (mn)	*165.2*	*320.5*	*3,643*	*3,822*
EBITDA	*130.0*	*269.1*	*1,582*	*3,063*
Net Income (mn)	*129.7*	*268.2*	*1,153*	*2,029*
EPS	*0.23*	*0.48*	*2.08*	*3.26*
EPS Growth	*42.3%*	*107.4%*	*331.3%*	*56.6%*
DPS	*N/A*	*N/A*	*N/A*	*N/A*
PER (x)	*63.6*	*30.7*	*7.1*	*4.5*
EV/EBITDA (x)	*214.2*	*103.5*	*22.3*	*11.5*
ROE	*2.7%*	*6.2%*	*21.1%*	*27.1%*
CFPS (op. CF)	*(0.66)*	*(0.82)*	*1.47*	*4.26*
P/CF (x)	*(22.3)*	*(18.1)*	*10.1*	*5.3*
Dividend Yield	*N/A*	*N/A*	*N/A*	*N/A*
FCF Yield	*-68.3%*	*-117%*	*7.1%*	*28.5%*
Net Debt / (Cash)	*7,602*	*24,402*	*2,221*	*1,474*

Figures in QAR, unless otherwise stated



Estimate Changes	*2007a*	*2008e*		*2009e*	
(QAR mn)		*Old*	*New*	*Old*	*New*
Revenue	*165.2*	*N/A*	*320.5*	*N/A*	*3,643*
EBITDA	*130.0*	*N/A*	*269.1*	*N/A*	*1,582*
EBITDA Margin (%)	*78.7*	*N/A*	*84.0*	*N/A*	*84.0*
Net Attrib. Income	*129.7*	*N/A*	*268.2*	*N/A*	*1,153*

Stock Data	
Last Dividend	*N/A*
Mkt.Cap / Shares (mn)	*QAR8,200 / 554*
Av. Mthly Liqd. (mn)	*QAR1,330*
52-Week High / Low	*QAR44 / 14.8*
Bloomberg / Reuters	*QGTS QD / QGTS.QA*
Est. free Float	*50%*

** prices as of 26 January, 2009*

I. BACKGROUND

COMPANY DESCRIPTION

The Qatar Gas & Transport Company, or 'Nakilat', which means transport in Arabic, was established in 2004 to build a large fleet of vessels to transport LNG produced from Qatar.

Qatar has the third-highest reserves of natural gas in the world and it is estimated the country will export 77 million tons of LNG annually by 2011e, making it the world's largest exporter of LNG. Long-term demand for natural gas is expected to remain robust, especially as it is the cleanest burning fossil fuel and many countries are changing their mix of energy use in favour of LNG to meet emission reduction targets.

By 2010e, Nakilat is expected to own 54 LNG vessels, 25 fully owned and 29 partially through JV partnerships. The vessels are being built for approximately USD11 billion with the latest technology for safe, reliable and cost effective transportation of gas. The larger Q Flex and Q Max ships have 50% and 80% more capacity than conventional LNG carriers. In addition to transporting LNG, Nakilat aims to operate in other sectors including shipyard repair, LPG and sulphur vessels.

STRATEGY

Nakilat has been awarded long-term charter contracts lasting approximately 25 years with an option to extend for a further five years. The group's primary role is to manage the fleet and to this end, management has entered into a strategic alliance with STASCO (Shell), a leading LNG operator, which will manage the LNG fleet with a view to training Nakilat's staff and handing over full control within 12 years.

We expect the group to take delivery of 18 LNG vessels in 2009e with a further four in 2010e. Consequently Nakilat's first full year of operation will be 2011. Until then, the key focus will be to ensure the timely delivery of all its ships.

RECENT RESULTS

Q3 results saw net income doubling y-o-y as the JV partners took delivery of 18 new vessels during the year, but the results are less meaningful at this stage as the business is still in its start-up phase. The 2008 full-year results should be more interesting as the group reports numbers for its fully owned LNG vessels for the first time. This should offer an insight into the revenue and cost dynamics of the LNG financial model.

OUTLOOK

While the long-term outlook for natural gas appears underpinned, the near-term picture is mixed. LNG prices are correlated to the oil price, and demand in the US waned earlier in the year as crude prices peaked. Furthermore, the International Energy Agency has warned that LNG production could fall behind demand from 2012 due to a lack of investment in new projects, particularly in Asia and Africa. In contrast, supply of LNG vessels is expected to increase to 370 vessels in 2013e. Currently there c.300 LNG carriers but there is enough supply for only 240 ships. The supply mismatch is expected to last for another five years and, as a result, LNG spot rates have dropped by a staggering 71% since August 2008.

With the above in mind, it is worth emphasising that Nakilat is not exposed to the spot market as it has long-term contracts. More importantly, its charterers, Qatar Gas and Rasgas also have long-term agreements to supply natural gas.

FORECAST

Due to the lack of disclosure, Nakilat forecasts are subject to relatively higher modelling risk in our view. That said, we should have more details following the publication of the 2008 FY results but for now we are using the following assumptions:

v) Daily rate of USD80k-USD110k.

vi) Voyage operating costs averaging 16% of sales.

Daily Rate

For the daily rate, we have used comparative figures from Golar Energy and Teekay LNG partners. For example, we estimate that Golar earns approximately USD50k to USD60k per day for its LNG vessels, which on average carry 80% less volume than Nakilat's larger vessels. Furthermore, Golar's fleet is not as technologically advanced, with some of the ships over 30 years old. With this in mind, we believe Nakilat should be able to command up to a 100% premium for its ships.

Voyage Operating Costs

Similarly on the cost side, Golar's vessel operating costs have historically averaged 20% of revenues. Given that Nakilat's vessel are estimated to be 40% more cost efficient than conventional LNG carriers, we expect operating costs to be significantly lower. However, we are erring on the side of caution and factoring in operating costs at 16% of sales.

II. VALUATION

Nakilat is highly geared and has attractive funding facilities. It also benefits from 25 year charter contracts which ultimately should give it the strongest revenue visibility within the sector. Consequently it enjoys the lowest WACC in our universe. Also we use a perpetual growth rate of 3.5% as we believe the group has strong pricing power due to the long term demand for LNG.

Figure 43: Discounted Cash Flow (DCF)
In QAR million, unless otherwise stated

	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	**(8,275)**	**(5,732)**	**574**	**2,104**	**2,418**	**2,535**	**2,637**	**2,742**	**2,852**	**2,966**
Change in Working Cap	(3)	(19)	(36)	(38)	(39)	(40)	(42)	(44)	(45)	(47)
Capex	(8,534)	(6,983)	(1,775)	(382)	(116)	(121)	(126)	(131)	(136)	(141)
FCF	**(8,268)**	**(5,419)**	**1,252**	**2,812**	**3,125**	**3,241**	**3,341**	**3,352**	**3,450**	**3,588**
Discount Factor	1.00	0.92	0.84	0.77	0.71	0.65	0.59	0.55	0.50	0.46
Discounted FCF	(8,268)	(4,970)	1,052	2,169	2,210	2,102	1,987	1,828	1,725	1,645
Perpetual Growth	3.50%									
WACC	9.0%									
PV of Cash Flows 2008-17e	1,481									
Terminal Value	**33,754**									
Total Firm Value	35,236									
Estimated Net (Debt) / Cash	(24,402)									
Total Equity Value	10,833									
No. of Shares (mn)	554									
LTFV per Share (QAR)	**19.6**									

Source: EFG-Hermes

Figure 44: Sensitivity Analysis
QAR per share, unless otherwise stated

Terminal Growth	WACC 7.0%	8.0%	9.0%	10.0%	11.0%
2.5%	50.5	27.0	10.2	N/A	N/A
3.0%	61.6	33.7	14.5	2.1	N/A
3.5%	75.9	41.9	**19.6**	5.5	N/A
4.0%	95.0	52.2	25.6	9.6	N/A
4.5%	121.8	65.3	33.0	14.3	0.6

Source: EFG-Hermes estimates

INITIATE WITH ST NEUTRAL /LT ACCUMULATE

The DCF implies a fair value of QAR19.6, which suggests upside potential of over 30%. However, it is worth noting that a 100 bps change in our WACC assumptions moves our fair value by over 20%. While the potential upside may not be as attractive as some of the other shipping stocks, we believe Nakilat's business model is more resilient as it is not subject to the perils of the spot market. Consequently we expect the stock to outperform in a downturn. Furthermore, we believe our forecasts are conservative and, even after factoring some modelling error, we suspect risks to our estimates weigh on the upside. In addition, we expect a payout ratio of 80% once the business is fully operational, which results in an attractive yield of 18.5% on our 2011e estimates.

While the valuation may appear compelling, the business is subject to significant execution risk, especially in the short term. For example, late delivery of vessels is still a possibility and there is no disclosure on the effect on Nakilat if the LNG plant is delayed. Currently we are assuming the vessels generate revenues from the date of delivery, but the ships could potentially be docked until the plant becomes operational, which will simply move our forecasts out.

Furthermore, Nakilat will need to raise an additional USD1 billion to fund its expansion plans and, while the company has had little difficulty in doing this in the past, it may be more difficult going forward as the market has tightened. That, said we expect the government of Qatar to provide financial support if necessary.

In summary, we are positive on Nakilat's long-term prospects and we believe the stock will be particularly attractive to value/income players given the generous payout ratio. However, we initiate with a ST Neutral / LT Accumulate recommendation with a view to being more positive once a) timely completion of the LNG plants are confirmed, b) more vessels are delivered and c) revenue / cost dynamics for fully owned vessels are published.

III. FINANCIAL FORECASTS

Income Statement (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Revenue	**165**	**321**	**1,885**	**3,643**	**3,822**
Change (%)	145%	94%	488%	93%	5%
COGS (excluding Depreciation)	0	(8)	(256)	(534)	(541)
as % of sales	*0%*	*2%*	*14%*	*15%*	*14%*
Gross Profit	**165**	**313**	**1,628**	**3,110**	**3,281**
Gross Profit Margin	100%	98%	86%	85%	86%
SG and A	(35)	(66)	(46)	(47)	(48)
as % of sales	*21%*	*20%*	*2%*	*1%*	*1%*
EBITDA	**130**	**269**	**1,582**	**3,063**	**3,233**
EBITDA Margin	79%	84%	84%	84%	85%
Depreciation	(0)	(10)	(331)	(691)	(701)
Net Operating Profit	130	259	1,251	2,372	2,531
Net Interest Expense	0	9	(98)	(342)	(356)
Minority Interest	1	1	1	2	3
Net Profit	**130**	**268**	**1,153**	**2,029**	**2,176**
EPS (QAR)	**0.23**	**0.48**	**2.08**	**3.26**	**3.46**

Source: Nakilat, EFG-Hermes estimates

Balance Sheet (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Cash & Liquid Assets	**2,475**	**967**	**967**	**1,880**	**3,667**
Accounts Receivable	96	136	136	136	136
Other Receivables	0	3	3	3	3
Net Accounts Receivable	96	139	139	139	139
Total Current Assets	**2,571**	**1,105**	**1,105**	**2,019**	**3,806**
Net Plant	0	2,032	18,535	24,347	24,347
Contract Work in Progress	9,382	17,133	8,047	4,096	4,051
Net Investments	2,457	2,384	2,644	2,644	2,644
Other Fixed Assets	1,677	2,375	2,375	2,375	2,375
Total Assets	**16,087**	**25,028**	**32,706**	**35,481**	**37,223**
Accounts Payable	191	207	207	207	1,739
Short Term Debt	0	616	7,282	8,207	8,207
Total Current Liabilities	**191**	**823**	**7,489**	**8,414**	**9,946**
Loans	**10,077**	**18,228**	**18,087**	**17,929**	**17,753**
Total Provisions	2	3	3	3	3
Fair Value Interest Rate Swap	1,022	1,656	1,656	1,656	1,656
Total Long Term Liabilities	11,101	19,887	19,746	19,588	19,412
Total Liabilities & Provisions	**11,292**	**20,710**	**27,235**	**28,002**	**29,358**
Shareholder's Equity	**4,796**	**4,318**	**5,472**	**7,478**	**7,864**
Total Liabilities & Equity	**16,089**	**25,028**	**32,706**	**35,481**	**37,223**

Source: Nakilat, EFG-Hermes estimates

Cash Flow Statement (December Year End)

In QAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Net Operating Profit	**130**	**268**	**1,153**	**1,806**	**1,902**
Depreciation & Amortisation	0	10	331	692	701
Other Operating Inflows (Outflows)	(497)	(731)	(673)	(340)	(269)
Net Cash Flow from Operating Activities	**(367)**	**(452)**	**812**	**2,158**	**2,334**
Cash Flow from Investing	**(5,156)**	**(10,417)**	**(7,337)**	**(2,212)**	**(387)**
Net Cash from Op. and Investing Activities	(5,524)	(10,869)	(6,525)	(54)	1,947
Net Cash Flow from Financing	**4,096**	**7,333**	**6,525**	**767**	**(176)**
Change in Cash	**(1,428)**	**(3,537)**	**0**	**713**	**1,771**

Source: Nakilat, EFG-Hermes estimates

NATIONAL SHIPPING CO. OF SAUDI ARABIA, NSCSA

29 JANUARY 2009

SAUDI ARABIA | SHIPPING

Short-Term Rec.: Sell	Current Price*: SAR 17.6
Long-Term Rec. : Neutral	LT Fair Value : SAR 14.9

We initiate on the National Shipping Company of Saudi Arabia (NSCSA) with a ST Sell and LT Neutral and a price target of SAR14.9, implying 15% potential downside.

- **NSCSA was Established in 1974 and is One of the Largest Global Vessel Operators.** The group is focused on container, LPG, Petrochemicals and Oil Tankers (VLCC). NSCSA has an experienced management team with an impressive track record. In addition, the group is financially sound with attractive funding facilities. Going forward, NSCSA aims to become a Top 5 global shipping company within four years.

- **The Group's Key Exposure is to the VLCC Market, which has seen Rates Fall by More Than 50% in the Last Quarter.** VLCCs generate more than 50% of annual revenues and NSCSA has seven out of 13 vessels in the spot market. Similarly the spot rates for chemical carriers (23.3% of sales) and containers (23.6% of sales) have fallen by c.40% in recent months and NSCSA has seven out of 16 chemical carriers and all its containers on the spot market.

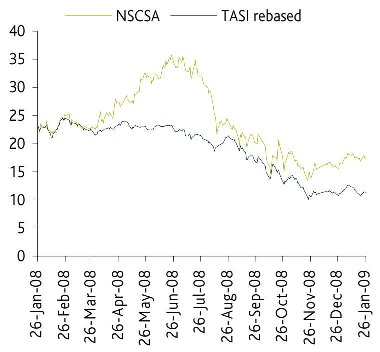
- **Vessels on Order Have Not Been Pre Chartered.** Alarmingly, the group has 16 chemical carriers and four VLCCs on order, which are due for delivery between 2009 and 2011 and none of the vessels have been pre-chartered. Consequently these ships will be exposed to the current (low) spot / charter rates or could be left idle should there be no demand. Furthermore, some of the current charter contracts are due for renewal in 2009 and in our view are likely to be renewed for c.20% below the existing agreement.

- **The Short-Term Outlook Appears Bleak and with Spot Prices Falling Across the Board.** We estimate NSCSA's revenues will decline 14% in 2009e despite taking delivery of four new VLLCs and four Chemical tankers. This results in an EPS decline of 41% in 2009e to SAR1.38. However, we expect revenues to increase by 20% in 2010e as spot rates recover and NSCSA benefits from a full year's ownership of the new vessels. Consequently we expect EPS to bounce by 24% to SAR1.71 in 2010e.

- **We Believe Negative Sentiment Could Hit the Shares.** Overall, due to its financial strength, we believe the group can weather the current storm and with the long-term industry fundamentals remaining strong, we believe NSCSA can fulfil its ambition of becoming a Top 5 global shipping company within four years. We expect the VLCC market to be more resilient during the downturn, which should benefit the group, and we suspect many operators may exit the market as the slowdown deepens. This should leave NSCSA in a strong position to benefit as and when the market recovers. However, short-term newsflow is likely to worsen which could drag the share lower in our view and with this in mind we are bearish for now.

December Year End	*2007a*	*2008e***	*2009e*	*2010e*
Revenue (mn)	*1,703*	*2,441*	*2,099*	*2,523*
EBITDA	*672.1*	*1,162*	*860.7*	*1,031*
Net Income (mn)	*422.6*	*740.3*	*433.1*	*535.8*
EPS	*1.48*	*2.35*	*1.38*	*1.71*
EPS Growth	*-24.4%*	*58.5%*	*-41.2%*	*23.7%*
DPS	*1.00*	*1.59*	*0.69*	*0.85*
PER (x)	*11.9*	*7.5*	*12.7*	*10.3*
EV/EBITDA (x)	*11.6*	*7.2*	*10.6*	*9.2*
ROE	*9.1%*	*14.6%*	*8.7%*	*10.1%*
CFPS (operating CF)	*1.66*	*3.18*	*2.95*	*3.26*
P/CF (x)	*10.6*	*5.5*	*6.0*	*5.4*
Dividend Yield	*5.7%*	*9.0%*	*3.9%*	*4.9%*
FCF Yield	*-10.6%*	*-10.5%*	*-5.0%*	*-0.5%*
Net Debt / (cash)	*1,555*	*2,508*	*3,319*	*3,572*

Figures in SAR, unless otherwise stated
*** Net Income and EPS for 2008 are actuals*



Estimate Changes (SAR mn)	*2007a*	*2008e Old*	*2008e New*	*2009e Old*	*2009e New*
Revenue	*1,703*	*N/A*	*2,441*	*N/A*	*2,099*
EBITDA	*672.1*	*N/A*	*1,162*	*N/A*	*860.7*
EBITDA Margin	*39.5%*	*N/A*	*47.6%*	*N/A*	*41.0%*
Net Attrib. Income	*422.6*	*N/A*	*740.3*	*N/A*	*433.1*

Stock Data	
Last Dividend	*SAR1 on 8 Apr 08*
Mkt. Cap / Shares (mn)	*SAR5,508 / 315*
Av. Mthly Liqd. (mn)	*SAR3,466*
52-Week High / Low	*SAR35.75 / 14.8*
Bloomberg / Reuters	*NSCSA AB / 4030.SR*
Est. free Float	*71.90%*

** prices as of 26 January, 2009*

I. BACKGROUND

COMPANY DESCRIPTION

The National Shipping Company of Saudi Arabia was established in 1974 and has grown to become one of the largest global shipping companies. NSCSA started as a containership owner/operator but subsequently expanded horizontally and is now focused in Crude, Chemical, LPG and General Cargo.

NSCSA's current portfolio consists of 13 oil tankers, 16 chemical tankers and four container vessels. In addition, the group has a further 16 chemical tankers and four oil tankers on order, which are due for delivery between 2009 and 2011.

The chemical operation is managed by National Chemical Carriers (NCC) which is 80% owned by NSCSA and 20% owned by SABIC. The group also owns 30.3% of LPG owner/operator Petredec Ltd.

STRATEGY

NSCSA's vessel portfolio is split c.40:60 in favour of the spot market. Ships on charter provide stable long-term recurring revenues and management actively switch ships on the spot market to higher yielding routes to maximise returns.

The group has a competitive advantage as it receives subsidised bunker (fuel) and is financially strong. We believe NSCSA has secured flexible funding at attractive rates and consequently will be in a strong position to consolidate should strategic assets come up for sale. Going forward, the group remains keen to expand within crude, petrochems and possible new sectors but is unlikely to grow its container division which is a competitive market.

Overall, we believe the group is in a strong position to weather the current storm and it remains on course to fulfil its target to become a global Top 5 shipping company within four years.

RECENT RESULTS

NSCSA has recently published its net income number for 2008. Overall net income rose 67% y-o-y but Q4 net income only grew by 2%, as spot rates dived in the quarter. We expect further details to be released in mid February 2008.

OUTLOOK

While FY results were positive, the outlook is less certain. Spot rates have fallen across the board and charter rates have also weakened. NSCSA has a material exposure to the spot market and is likely to see revenues fall in 2009e. The liner and petrochemical market are more geared to economic growth and are most at risk from continued price weakness. VLCCs should be more resilient due to oil demand being relatively inelastic. Furthermore, NSCSA has a cost advantage and should be able to compete more effectively in this market.

Figure 45: Forecasts
In SAR million, unless otherwise stated

	2007a	2008e	2009e	2010e
Revenues				
Very Large Crude Carriers	741	1,319	1,321	1,583
% Change		*78.1%*	*0.2%*	*19.8%*
Liner Service	488	561	303	333
% Change		*14.9%*	*-46.0%*	*10.0%*
Petrochemical Carriers	474	542	475	607
% Change		*14.3%*	*-12.5%*	*27.8%*
Total Revenues	**1,703**	**2,423**	**2,099**	**2,523**
% Change		*42.2%*	*-13.4%*	*20.2%*
Operating Income				
Very Large Crude Carriers	261	681	476	570
Margin		*51.6%*	*36.0%*	*36.0%*
Liner Service	109	147	67	73
Margin		*26.1%*	*22.0%*	*22.0%*
Petrochemical Carriers	82	93	66	85
Margin		*17.1%*	*14.0%*	*14.0%*
Total Operating Profit	**451**	**920**	**609**	**728**
Total Margin	*26.5%*	*38.0%*	*29.0%*	*28.9%*

Source: EFG-Hermes

NSCSA is highly geared to the performance of the VLCC market as it accounts for more than 50% of its revenues. Going forward, we expect the VLCC market to remain difficult throughout 2009. We are estimating 0.2% revenue growth for VLCCs in 2009e despite the addition of two new vessels during the year, which means that on a like-for-like basis we are forecasting a revenue decline of 15%. Beyond 2009, we expect the market to stabilise and the division should report stronger growth (20%) in 2010e as it benefits from a full year's vessel ownership.

The Petrochemicals group has nine vessels on charter and seven in a polling agreement (similar to spot). Overall on a like for like basis, we expect revenues to fall 22% and decline by 12.5% absolutely as it takes delivery of two new vessels.

We believe the liner/container market will be very weak in 2009 as it is a competitive industry and supply of vessels is expected to increase by double digits. Overall we expect revenues to drop 46% in 2009e before recovering in 2010e.

In summary, we expect revenues to fall by 13.4% in 2009e, versus 42% growth in 2008e. However, we do expect a more stable market in 2010e when the group should benefit from the delivery of VLCC and chemical vessels.

We estimate operating margins will contract 900 bps in 2009e, and a further 10 bps in 2010e. Below operating income, finance charges jump by more than 50% in 2009e as the group takes on more debt as the vessels are delivered. Overall, we estimate that NI and EPS will fall 41% in 2009e before rebounding 24% in 2010e.

II. VALUATION

Figure 46: Discounted Cash Flow (DCF)
In SAR million, unless otherwise stated

	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	**1,162**	**861**	**1,031**	**1,124**	**1,136**	**1,114**	**1,142**	**1,253**	**1,303**	**1,355**
Change in Working Cap	115	48	5	(17)	16	(13)	(1)	(1)	(1)	(1)
Capex	(1,570)	(1,200)	(1,049)	(1,576)	(287)	(147)	(150)	(157)	(163)	(169)
FCF	**(294)**	**(291)**	**(13)**	**(469)**	**865**	**955**	**991**	**1,095**	**1,139**	**1,184**
Discount Factor	1.00	0.89	0.80	0.71	0.64	0.57	0.51	0.45	0.40	0.36
Discounted FCF	(294)	(260)	(10)	(334)	607	563	555	516	479	441
Perpetual Growth	3.0%									
WACC	12.0%									
PV of Cash Flows 2008-17e	2,263									
Terminal Value	**4,912**									
Total Firm Value	7,175									
Estimated Net (Debt) / Cash	(2,508)									
Total Equity Value	4,667									
No. of Shares (mn)	313									
LTFV per Share (SAR)	**14.9**									

Source: EFG-Hermes

For our DCF calculation we have used the following assumptions:

vii) Cost of Equity of 14.3%

viii) Cost of debt at 5%

ix) Total WACC 12.0%

x) Terminal growth of 3%

Figure 47: Sensitivity Table
In SAR, unless otherwise stated

		WACC				
		10.0%	**11.0%**	**12.0%**	**13.0%**	**14.0%**
Terminal Growth	**2.0%**	21.0	16.7	13.3	10.5	8.2
	2.5%	22.4	17.7	14.0	11.0	8.6
	3.0%	24.0	18.8	**14.9**	11.7	9.1
	3.5%	25.8	20.1	15.7	12.3	9.6
	4.0%	27.9	21.5	16.8	13.1	10.2

Source: EFG-Hermes

INITIATE WITH ST SELL / LT NEUTRAL

The DCF implies a fair value of SAR14.9, which suggests downside of 15%. Consequently we remain cautious in the short term as NSCSA has significant exposure to the spot market, which could deteriorate further. In addition, unlike some of the other operators, the group's vessels on order have not been pre-chartered. As a result, there is no guarantee of the new vessels generating revenues as they will be at the mercy of the spot market, which poses another risk in the short term.

That said, NSCSA is in a sound position from a financial perspective with an experienced management team. We expect the group to weather the current storm and emerge as a stronger business. NSCSA has a sensible business model in our view and is likely to benefit as and when the market recovers. The operational gearing should mean healthy upgrades when the spot market bounces back and vis-à-vis performance in the share price, but things could get worse before they get better and therefore we remain cautious in the near term.

III. FINANCIAL FORECASTS

Income Statement (December Year End)

In SAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Revenue	**1,703**	**2,441**	**2,099**	**2,523**	**2,838**
Change	3%	43%	-14%	20%	12%
COGS (excluding Depreciation)	(1,031)	(1,279)	(1,238)	(1,492)	(1,714)
Gross Profit	**672**	**1,162**	**861**	**1,031**	**1,124**
Gross Profit Margin	39%	48%	41%	41%	40%
SG and A	(87)	(107)	(84)	(101)	(114)
As % of Sales	*5%*	*4%*	*4%*	*4%*	*4%*
EBITDA	**672**	**1,162**	**861**	**1,031**	**1,124**
EBITDA Margin	39%	48%	41%	41%	40%
Depreciation	221	242	252	303	341
Net Operating Profit	451	920	609	728	783
Net Interest Expense	(128)	(119)	(201)	(212)	(210)
Non-operating Income	72	7	9	8	4
Minority Interest	(4)	(8)	(6)	(8)	(11)
Net Profit	**423**	**740**	**433**	**536**	**576**
EPS (SAR)	**1.48**	**2.35**	**1.38**	**1.71**	**1.84**

Source: NSCSA, EFG-Hermes estimates

Balance Sheet Statement (December Year End)

In SAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Cash & Liquid Assets	**877**	**989**	**862**	**832**	**33**
Accounts Receivable	192	293	252	303	341
Other Receivables	14	25	25	25	25
Net Accounts Receivable	206	317	276	327	365
Inventory	89	90	124	151	193
Prepaid Expenses	49	64	64	64	64
Other Current Assets	180	124	133	139	146
Total Current Assets	**1,401**	**1,584**	**1,458**	**1,513**	**800**
Net Plant	4,634	4,751	6,517	7,954	10,155
Contract Work in Progress	1,262	2,474	1,656	966	0
Net Investments	234	309	332	355	377
Other Fixed Assets	266	250	198	356	407
Total Assets	**7,797**	**9,368**	**10,161**	**11,144**	**11,728**
Accounts Payable	324	398	390	467	536
Incomplete Voyages	28	32	32	32	32
Current portion of Short Term Loan	203	364	418	430	430
Dividends Payable	18	24	24	24	24
Provisions	143	150	153	153	154
Total Current Liabilities	**717**	**967**	**1,016**	**1,106**	**1,175**
Loans	**2,229**	**3,133**	**3,762**	**3,975**	**3,938**
Tax Provisions	10	6	6	6	6
Total Liabilities & Provisions	**2,983**	**4,136**	**5,002**	**5,653**	**5,889**
Minority Interest	154	162	168	175	186
Shareholder's Equity	**4,660**	**5,070**	**4,991**	**5,316**	**5,652**
Total Liabilities & Equity	**7,797**	**9,368**	**10,161**	**11,144**	**11,728**

Source: NSCSA, EFG-Hermes estimates

Cash Flow Statement (December Year End)
In SAR million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Net Profit	**423**	**740**	**433**	**536**	**576**
Depreciation & Amortization	270	306	325	399	460
Other Operating inflows (outflows)	(173)	(51)	165	85	58
Net Cash Flow from Operating Activities	**519**	**995**	**923**	**1,020**	**1,093**
Cash Flow from Investing	**(1,094)**	**(1,671)**	**(1,281)**	**(1,153)**	**(1,695)**
Net Cash from Op. and Investing Activities	(575)	(676)	(359)	(133)	(602)
Net Movement in Loans	60	1,127	731	320	70
Net Cash Flow from Financing	**1,263**	**814**	**231**	**104**	**(198)**
Change in Cash	**688**	**137**	**(127)**	**(29)**	**(800)**

Source: NSCSA, EFG-Hermes estimates

GULF NAVIGATION

29 JANUARY 2009

UAE | SHIPPING

Short-Term Rec.: Accumulate	Current Price*: AED 0.60
Long-Term Rec. : Neutral	LT Fair Value : AED 0.77

We initiate on Gulf Navigation with a ST Accumulate / LT Neutral recommendation and a LT Fair Value of AED0.77, implying 28% upside.

- **Gulf Navigation was Founded in 2001 and is a Pure Play Ship Owner/Operator**. The group operates in the bulk and wet markets and is expected to manage 14 vessels by the end of 2009. In addition to the ship chartering business, GNH owns a ship agency service, ship management, and marine product and distribution businesses. These are relatively new business lines and remain in their infancy.

- **Gulf Navigation Lacks Scale.** The group has ambitions to become a leading shipping company in the region but we suspect it will struggle to make a significant impact in the near term due to a lack of scale. The core shipping business will only have 14 vessels by end-2009 and the other business lines do not generate significant revenues as of yet. The group will need to step up its investment/acquisition plans if it wants to compete effectively but acquiring in the current market makes little sense in our view as the yields are low and the outlook is uncertain.

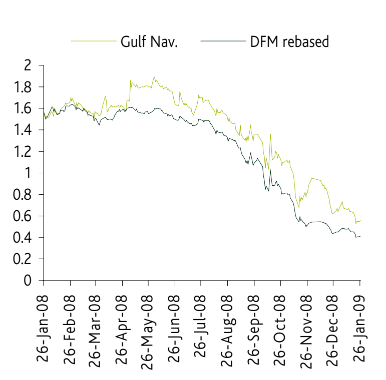
- **We Expect 2009e to be a Difficult Year for GNH** as the top line comes under pressure with renewal rates coming down 20% on five charter contracts, according to our estimates. This results in revenue growth of 5.4% in 2009e despite the addition of three new vessels during the year. As a result, we forecast a significant reduction in the bottom line with 2009e EPS dropping 32% due to higher financing charges.

- **Buyback and Dividend Could Boost the Shares.** On a more positive note, Gulf Nav has announced plans for a half-year dividend and a 10% share buyback, which should be circa 11% EPS accretive at the current price. We view this move as positive as it should boost the shares in the short term and offer confidence in the group's longer-term outlook. More importantly, we believe it signals the end of any significant expansion plans, which is reassuring, given the tough market conditions.

- **Attractive Yield Provides Downside Support**. While the outlook may be difficult, we believe the shares will hold up well going forward given the attractive yield (12.3%). In addition, the group has little exposure to the spot market, which should mean that our forecasts are relatively underpinned. Furthermore, we expect to see some M&A activity in the market next year and Gulf Navigation could be a primary target.

December Year End	*2007a*	*2008e*	*2009e*	*2010e*
Revenue (mn)	*272.1*	*415.8*	*438.1*	*487.4*
EBITDA	*142.8*	*238.9*	*236.8*	*263.1*
Net Income (mn)	*116.0*	*173.1*	*117.1*	*141.3*
EPS	*0.07*	*0.10*	*0.07*	*0.09*
EPS Growth	*-*	*49%*	*-32%*	*21%*
DPS	*0.07*	*0.07*	*0.07*	*0.08*
PER (x)	*8.6*	*5.7*	*8.5*	*7.0*
EV/EBITDA (x)	*9.9*	*5.9*	*8.1*	*6.9*
ROE	*6.5%*	*9.5%*	*6.4%*	*7.7%*
CFPS (operating CF)	*0.10*	*0.15*	*0.12*	*0.14*
P/CF (x)	*5.8*	*3.9*	*5.2*	*4.4*
Dividend Yield	*11.7%*	*12.3%*	*12.3%*	*12.9%*
FCF Yield	*-30.8%*	*-21.8%*	*-28.5%*	*17.7%*
Net Debt / (Cash)	*(86.0)*	*(414.8)*	*(917.3)*	*(833.4)*

Figures in AED, unless otherwise stated



Estimate Changes	*2007a*	*2008e*		*2009e*	
(AED mn)		*Old*	*New*	*Old*	*New*
Revenue	*272.1*	*N/A*	*415.8*	*N/A*	*438.1*
EBITDA	*142.8*	*N/A*	*238.9*	*N/A*	*236.8*
EBITDA Margin	*52.5%*	*N/A*	*57.5%*	*N/A*	*54.0%*
Net Attrib. Income	*116.0*	*N/A*	*173.1*	*N/A*	*117.1*

Stock Data	
Last Dividend	*AED0.07 on 08 April 08*
Mkt.Cap / Shares (mn)	*AED993 / 1,655*
Av. Mthly Liqd. (mn)	*AED1,079*
52-Week High / Low	*AED1.89 / 0.6*
Bloomberg / Reuters	*GULNAV:UH/GNAV.DU*
Est. free Float	*55%*

** prices as of 26 January, 2009*

I. BACKROUND

Gulf Navigation is a pure play ship owner/operator. The group currently operates 11 vessels and expects to take delivery of three more ships before the end of 2009. In the mix, GNH owns / will own either fully or partly six chemical ships, which are on long-term charters, and seven oil tankers, which are all on short-term charters.

In addition to the ship chartering business, GNH owns a ship agency service, ship management, and marine product and distribution businesses. These relatively new business lines remain in their infancy.

GNH was originally founded in Oman in 2001 before relocating to Dubai in 2003. GNH listed on the DFM in February 2007, offering 55% of its share capital and raising AED910 million (c.USD250 million).

STRATEGY

Gulf Navigation's vision is to become the largest shipping company in the Middle East by focussing on customer service and building long-term client relationships. The group aims to deploy its vessel portfolio through a mixture of long- and short-term charters, with the long-term charters providing guaranteed recurring revenue, and short-term deals offering potentially higher yields.

Furthermore, the group aims to take advantage of the current downturn by acquiring ships for knockdown prices as and when distress sellers come to the market. However, following the announcement of a share buyback programme, we see little headroom for significant expansion, especially given that the group has to finance the purchase of four chemical vessels.

RECENT RESULTS

Recent Q3 numbers saw revenues growing by c.70% y-o-y and net income more than doubling from AED20.3 million to AED43.9 million due to the addition of two new vessels. However, the q-o-q comparison offers a better insight in our view. For example, revenues were flat q-o-q despite the addition of a new vessel and benefitting from a full quarter's contribution from the chemical vessel added in late Q208. This suggests that some charter contracts have been renewed at lower rates.

More recently, the group has announced a 10% share buyback and we estimate this will be c.11% EPS accretive at the current share price.

FORECAST

We estimate Gulf Navigation had five vessels due for charter renewal in Q3/Q4 2008, which is unfortunate from a timing perspective as both the charter and spot markets have deteriorated sharply in recent months. On average, we estimate the renewal rate will be 20% down. This results in revenue growth of only 5.4% in 2009e, despite the addition of three new vessels. The capex payment for the four new chemical vessels increases net debt to AED970 million from AED440 million, leading to finance costs rising more than 50% in 2009e. This results in an estimated y-o-y EPS fall of 32% from AED 0.10 to AED 0.07, leaving the stock trading on 8.5x 2009e P/E.

RISKS

The key risk to Gulf Navigation is from the charter renegotiations as discussed above, and the potential late delivery of the chemical carriers. The chemical carriers have been pre chartered and consequently will start generating revenues immediately after delivery. Any delay will simply push out our forecasts.

II. VALUATIONS

Gulf Nav is a pure ship owner/operator and we use a DCF valuation to determine fair value

Figure 48: Discounted Cash Flow (DCF)
In AED million, unless otherwise stated

	2008e	2009e	2010e	2011e	2012e	2013e	2014e	2015e	2016e	2017e
EBITDA	**239**	**237**	**263**	**256**	**248**	**216**	**222**	**229**	**240**	**250**
Change in Working Cap	28	6	7	1	1	-4	0	0	0	0
Capex	(496)	(477)	(49)	(49)	(50)	(26)	(26)	(27)	(29)	(30)
FCF	**(229)**	**(234)**	**221**	**208**	**199**	**186**	**196**	**202**	**212**	**220**
Discount Factor	1.00	0.90	0.81	0.74	0.66	0.60	0.54	0.49	0.44	0.40
Discounted FCF	(229)	(211)	180	153	124	117	109	103	97	90
Perpetual Growth	3.0%									
WACC	10.8%									
PV of Cash Flows 2008-17e	533									
Terminal Value	**1,162**									
Total Firm Value	1,695									
Estimated Net (Debt) / Cash	-415									
Total Equity Value	1,280									
No. of Shares (mn)	1,655									
LTFV per Share (AED)	**0.77**									

Source: EFG-Hermes

Figure 49: Sensitivity Analysis
In AED, unless otherwise stated

		WACC				
		8.0%	**9.0%**	**10.8%**	**12.0%**	**13.0%**
Terminal Growth	**2.00%**	1.29	1.02	0.69	0.54	0.43
	2.50%	1.39	1.09	0.73	0.56	0.45
	3.00%	1.52	1.17	**0.77**	0.59	0.47
	3.50%	1.67	1.27	0.82	0.62	0.50
	4.00%	1.86	1.38	0.87	0.66	0.53

Source: EFG-Hermes

INITIATE WITH ST ACCUMULATE / LT NEUTRAL RECOMMENDATION AND AED0.77 FV

Our DCF valuation suggests a fair value of AED0.77, implying 28% upside.

Gulf Nav IPO'd in 2003 with aggressive growth plans, which have not quite materialised. The group initially expected to manage 26 vessels within five years, which compares with 14 that it will now have by the end of 2009. Perversely, we believe this will prove to be positive for shareholders as the group has less exposure to a weak industry, making it more attractive as a consolidation candidate.

Gulf Navigation's fleet are on short- and long-term charters, with only one vessel exposed to the spot market. This provides some confidence in our forecasts. Going forward, we expect the market to consolidate and, with Gulf Nav lacking real scale, we suspect the group could become an M&A target. This combined with an attractive yield of 12.3% leads us to initiate with a ST Accumulate and LT Neutral recommendation.

III. FINANCIAL FORECASTS

Income statement (December Year End)

In AED million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Revenue	**272**	**416**	**438**	**487**	**495**
Change	-	53%	5%	11%	2%
COGS (excluding Depreciation)	(111)	(150)	(171)	(191)	(203)
As a % of Sales	*41%*	*36%*	*39%*	*39%*	*41%*
Gross Profit	**162**	**266**	**267**	**296**	**292**
Gross Profit Margin	59%	64%	61%	61%	59%
SG and A	(19)	(27)	(31)	(33)	(37)
As a % of sales	*7%*	*7%*	*7%*	*7%*	*7%*
EBITDA	**143**	**239**	**237**	**263**	**255**
EBITDA Margin	52%	57%	54%	54%	52%
Depreciation	46	52	57	64	64
Net Operating Profit	97	187	180	200	191
Net Interest Expense	(28)	(42)	(64)	(58)	(52)
Non-Operating Income	47	28	2	(1)	(1)
Net Profit	**116**	**173**	**117**	**141**	**138**
EPS	**0.07**	**0.10**	**0.07**	**0.09**	**0.08**

Source: Gulf Navigation, EFG-Hermes estimates

Balance Sheet Statement (December Year End)

In AED million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Cash & Liquid Assets	**737**	**550**	**44**	**1**	**6**
Accounts Receivable	35	54	57	63	64
Net Accounts Receivable	35	54	57	63	64
Inventory	4	3	7	7	7
Total Current Assets	**776**	**607**	**108**	**72**	**78**
Net Plant	1,333	1,777	2,196	2,181	2,167
Gooodwill	582	520	513	560	564
Total Assets	**2,690**	**2,904**	**2,896**	**2,800**	**2,783**
Accounts Payable	57	104	110	122	124
Other Payables	34	12	6	6	6
Total Payables	91	116	115	128	130
Current Portion of Short term loan	86	100	97	35	55
Total Current Liabilities	177	217	213	162	184
Loans	**737**	**864**	**864**	**800**	**749**
Total non-current Liabilities	**737**	**864**	**864**	**800**	**749**
Total Liabilities & Provisions	914	1,081	1,077	962	934
Shareholder's Equity	**1,776**	**1,823**	**1,819**	**1,838**	**1,849**
Total Liabilities & Equities	**2,690**	**2,904**	**2,896**	**2,800**	**2,783**

Source: Gulf Navigation, EFG-Hermes estimates

Cash Flow Statement (December Year End)

In AED million, unless otherwise stated

	2007a	2008e	2009e	2010e	2011e
Net Operating Profit	**134**	**173**	**117**	**141**	**139**
Depreciation & Amortization	46	52	57	64	64
Other Operating inflows (outflows)	(7)	28	17	20	15
Net Cash Flow from Operating Activities	**172**	**253**	**191**	**225**	**218**
Cash Flow from Investing	**(1,015)**	**(481)**	**(475)**	**(49)**	**(51)**
Net Cash from Op. and Investing Activities	(843)	(228)	(283)	176	167
Net Mouvement in Loans	625	161	(100)	(97)	(35)
Net Cash Flow from Financing	**943**	**41**	**(222)**	**(219)**	**(162)**
Change in Cash	**101**	**(187)**	**(505)**	**(43)**	**5**

Source: Gulf Navigation, EFG-Hermes estimates

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Accumulate	10 to 25%
Neutral	(10%) to 10%
Reduce	(10%) to (25%)
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