

Mabaneer

Equity Research Update

Sector – Real Estate

Awaiting next growth runway – downgrade to Neutral

Covid delays operational ramp-up & growth runway; downgrade to Neutral

Covid related shutdowns caused delays in the operational ramp-up of Mabaneer's Kuwait operations. This led to a slower progression in attaining higher occupancy rates for Phase IV-retail at Avenues Kuwait, and intensified retail sales competition from growing market-shares of e-tailers. Further, hotel operations were interrupted, as the completion of 5-Star Waldorf Astoria's construction was delayed, and the 4-Star Hilton Garden Inn achieved lower occupancy rates. We downgrade the stock to 'Neutral', until the next growth runway and capex outlay are more visible, while existing and planned operations reach its stabilized full potential. The company's share price could see gains in the lead up to Kuwait's MSCI upgrade by end Nov-2020, given the stock's flows/ADVT multiple of 46.8x, based on the 3M-ADVT (Jul-Sept 2020).

Securing full potential Phase-IV Retail +Hotel operations is immediate priority

Kuwait's Grade-A retail space is forecasted to grow by 18.8% y-o-y to 967,500 sq.m by 2021E, as per REMI. Average rents for Grade-A spaces are forecasted to drop 5.5%, but this should keep occupancy rates relatively healthy at 92% in 2021E, as the market remains price sensitive. For Mabaneer, we now forecast group revenues of KWD 64.1 Mn for 2020E, and KWD 105.0 Mn and KWD 107.5 Mn for 2021E and 2022E respectively. We recalibrate our forecasts mainly from the impact of Covid, and now assume a blended average rent of KWD 19.8/sq.m per month, down ~3% from our previous estimate. We keep average occupancy rates at 92% over 2020E-2022E. For the hotels segment, we now forecast a lower full potential revenue of KWD 8.2 Mn by 2022E, (previous forecast: KWD 11 Mn), driven by forecasted average occupancy rates of 45.5%, which we remain comfortable with at this point in time.

Growth capex allocation in new paradigm requires a rethink

We view Mabaneer's decision in mid-Aug 2020 to restudy their Avenues Riyadh project constructively, given the significant change in business environment with the onset of Covid, and the significant size of the project, which includes a mall space GLA of 400,000 sq.m and four multi-purpose towers. We remain positive on Mabaneer's capital allocation track record thus far, given their ability to put high quality assets in the market, and achieve above-market retail rents along with high margins from those existing projects. Nevertheless, we prefer to see more visibility for Mabaneer's capex growth-runway of other regional projects, and their Salmiya project before including them in our forecasts and valuation.

Valuation & Risks – Lowering TP to KWD 0.715/share

Our revised target price (TP) of KWD 0.715/share is based on a 70:30 blend of DCF and 2021E P/NAV valuation. **Key upside risks:** 1) Quicker achievement of full potential operations in Kuwait 2) Faster capex-led growth and growth accretive e-commerce acquisitions **Key downside risks:** 1) Continuation of Covid, driving lower footfalls and retail sales conversion 2) Oversupply in retail and prospective real estate segments 3) Significant cost over-runs for ongoing and future projects.

Key Financials	2018	2019	2020E	2021E	2022E
Revenue (KWD Mn)	85.4	96.4	64.1	105.0	107.5
GPM (%)	79.1%	77.0%	64.4%	75.1%	74.7%
EBIT (KWD Mn)	56.5	62.2	27.3	64.8	66.2
Net Income (KWD Mn)	52.5	56.4	22.2	57.8	59.2
EPS (KWD)	0.050	0.051	0.020	0.052	0.054
PE (x)	10.7	16.7	37.5	14.4	14.0
PB (x)	1.4	2.0	1.7	1.5	1.4
Div. yield (%)	1.7%	1.1%	0.7%	2.0%	2.0%

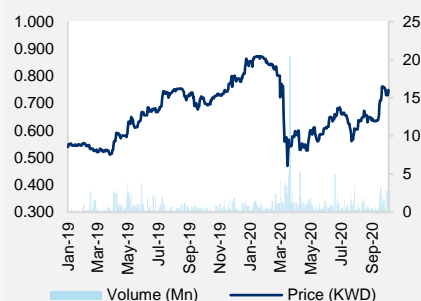
Sources: Kamco Invest Research and Mabaneer

Neutral

CMP 05-Oct-20: KWD 0.753

Target Price: KWD 0.715

Upside/Downside: -5.1%



Price Perf.	1M	3M	12M
Absolute	2.6%	-3.9%	-13.0%
Relative	-2.5%	-12.7%	-12.3%

Stock Data

Bloomberg Ticker	MABANEE KK
Refinitiv Ticker	MABK.KW
Last Price (KWD)	0.753
MCap (KWD Mn)	832
MCap (USD Mn)	255
EV (KWD Mn)	1,105
Stock Performance - YTD (%)	-11.8%
PE - 2020E (x)	37.5
PB - 2020E (x)	1.7
Dividend yield - 2020E (%)	0.7%
52-Week Range (KWD)	0.470 / 0.873

Sources: Kamco Invest Research & Bloomberg

Thomas Mathew

Assistant Vice President

+ (965) 2233 6741

tmathew@kamcoinvest.com

Valuation and Risks

Target price cut to KWD 0.715/share; downgrade to 'Neutral' rating

We reworked our forecasts post attending Mabanee's H1-20 earnings conference call and cut our group EPS forecasts by around 68% and 17% respectively for 2020E and 2021E. Key drivers for our lower forecasts are 1) the impact of Covid and related shutdowns in 2020E for all components, 2) slower ramp-up of Phase IV revenue generation 3) lower blended rents for Phase I-IV over 2020E-2022E and 4) delays in the start date of 5-Star Waldorf Astoria and the impact of Covid-19 on occupancy rates and ADRs of 4-Star Hilton Garden Inn. Our revised target price (TP) of KWD 0.715/share (Previous: KWD 0.740/share) is based on a 70:30 blend of DCF and 2021E P/NAV valuation. We downgrade the stock to 'Neutral' until the next growth runway and capex strategy are more visible, while existing and planned operations reach its stabilized full potential. Further, post rallying over 60% from its Mar-2020 lows, our TP adequately captures the fundamentals of the company in the current environment, which does not represent a significant change (-5.1%) to the current market price of the company (KWD 0.753/share).

Mabanee Fair Value			
Valuation Method	Fair value per share (KWD)	Weight (%)	Weighted Value (KWD)
DCF	0.700	70%	0.490
P/NAV - 2021E	0.750	30%	0.225
Weighted Average Fair Value per Share (KWD)			0.715
Current market price (KWD)			0.753
Upside/Downside			-5.1%

Sources: Kamco Invest Research

In our DCF valuation, we have assumed a terminal growth rate of 1.5%, and average WACC of 7.5% over our forecast period, which we believe appropriately represents the sustainable long-term growth rate and risk profile for the company, given the nature of technological advancement and disruption in the sector. We also model the impact of IFRS-16 'Leases on all operational metrics for our financial forecasts. For the terminal value, we have assumed a return on new investment capital (RONIC) that is comparable to the terminal year WACC. Our valuation includes Phase I and Phase II of Avenues Bahrain, including the hotel project, at 35% associate participation. Fair values of land in Saudi, land in Salmiya, and the Fintas project are included in our valuation.

Retail sector disruption ongoing; but Kuwait operations still positive

Our valuation based on 2021E P/NAV derives a price of KWD 0.750/share based on a multiple of 0.85x 2021E NAV, which is fair in our view, given 1) the level of disruption caused by the increasing market share of e-tailing, 2) newer business models evolving in other RE segments which Mabanee aims to foray into, and 3) when compared with closer industry peers in the region.



Sources: Kamco Invest Research, Mabanee

We remain positive on Mabanee's Kuwait operations (including hotels) reaching full potential on an annualized basis by 2022E, barring any re-occurrence of Covid related shutdowns to Avenues Kuwait, and other unforeseen circumstances. Avenues continues to remain the retail and entertainment destination of choice in Kuwait, and post-Covid, we expect Hotel revenues to pickup from higher occupancy rates and ADRs, which should drive FCF conversions rates towards 100%.

In the near term, Mabanee's shares should benefit from MSCI's upgrade of Kuwait to EM status, given the stock's high flows/ADVT multiple of 46.8x, based on the company's 3M-ADVT (Jul-Sept 2020) according to our estimates.

Upside/downside risks to our rating & forecasts include:

Upside risks:

- Rebound of Kuwait & GCC economic growth and discretionary consumer spending
- Quicker achievement of full potential operations in Kuwait
- Faster capex-led growth, and growth via accretive e-commerce acquisitions

Downside risks:

- Continuation of Covid driving lower footfalls and retail sales conversion
- Slowdown of GCC economic growth and discretionary consumer spending
- Oversupply of retail spaces and other prospective RE segments
- Significant cost over-runs of development costs of expansion projects

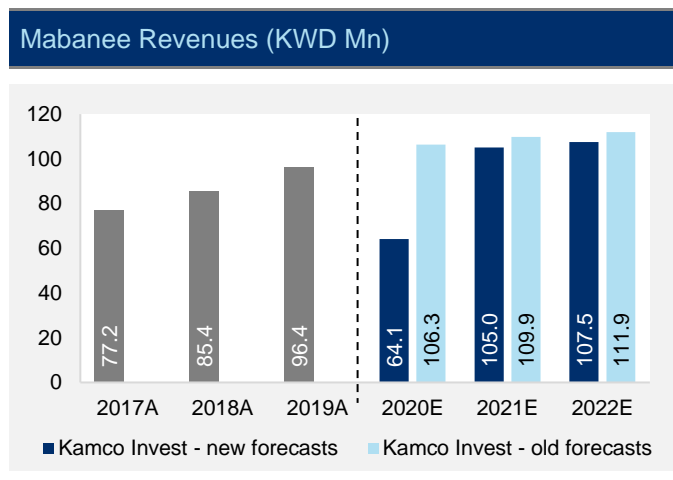
Investment Thesis

Realization of full potential Kuwait operations delayed

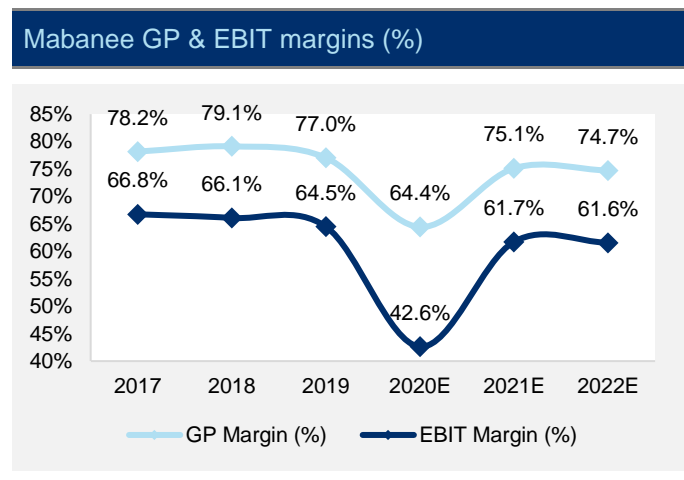
The onset of Covid has caused significant delays for full potential revenue realization at Mabaneer's Kuwait Phase IV retail and hotel operations. In our earlier update (*Mabaneer – Still reason to shop*), we expected Phase IV to reach full potential occupancy rates of 95% by end Q4-19/early Q1-2020 and forecasted average rental revenues of around KWD 82 Mn for 2020E and 2021E. However, Avenues Kuwait was shutdown to limit the impact from Covid from mid-Mar 2020 until end Jun-2020, following the government's instructions. Further, the company management mentioned that Phase IV occupancy rates was 94%, but occupancy rates based on rental revenues received reached ~80% at the end of H1-2020. Further it was highlighted that overall occupancy rate was down ~2% from 95% at the end of Q4-2019 for revenue generating leased spaces. Mabaneer also guided for a revenue loss of KWD 40 Mn for 2020 as a result, and further reiterated the guidance in their H1-2020 conference, mainly due to the following initiatives from the company for each of its components:

- Discounts of 100% for F&B, and 25% for retail tenants from mid-Mar 2020 until end-Mar 2020
- Full rent waiver from Apr- Jun 2020 for all tenants
- Partial 50% rent waiver across tenants for the months of Jul-Aug 2020
- Closure of entertainment, cinemas and FEC units till date
- Shutdown of Hilton Garden from Mar-2020 until 28 Jul 2020

We now forecast group revenues of KWD 64.1 Mn for 2020E, and KWD 105.0 Mn and KWD 107.5 Mn for 2021E and 2022E, respectively which are lower than our previous estimates. Our lower forecasts now reflect 1) the impact of Covid and related shutdowns in 2020E for all components, 2) slower ramp-up of Phase IV revenue generation 3) lower blended rents for Phase I-IV over 2020E-2022E and 4) delays in the start date of 5-Star Waldorf Astoria and the impact of Covid-19 on occupancy rates and ADRs of 4-Star Hilton Garden Inn.



Source: Kamco Invest Research, Mabaneer



Source: Kamco Invest Research, Mabaneer

We recalibrate our forecasts mainly from the impact of Covid, and now assume a blended average rent of KWD 19.8/sq.m per month down ~3% from our previous estimate: KWD 20.2/sq.m per month. We keep average occupancy rates of Phase I-IV at 92% over 2020E-2022E. For the hotels segment, we forecast lower full potential revenues of KWD 8.2 Mn in 2022E, as against our earlier forecast of KWD 11 Mn, driven by average occupancy rates of 45.5%, which we remain comfortable with at this point in time. We retain our ADR estimates of KWD 110/night and KWD 70/night for the 5-Star and 4-Star hotels, given the considerable lead time until 2022E.

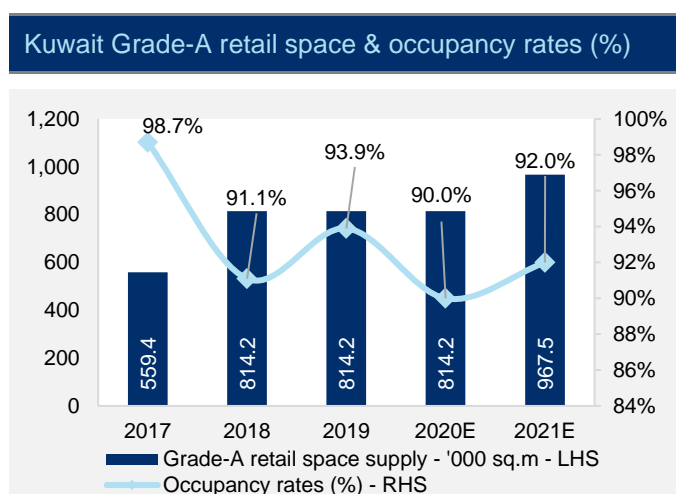
Margins in 2021 and 2022 to be lower by 200bps to 300bps

GP margins and EBIT margins are forecasted to fall significantly from 77% and 64.5% respectively in 2019 to 64.4% and 42.6% in 2020E as per our forecasts, from the impact of Covid on revenues primarily. Further, we expect GP margins (~75% avg) and EBIT margins (~61% avg) to be lower by 200bps-300bps in 2021E and 2022E, driven by the higher revenue integration of lower margin hotel operations (GOPPAR: 44%), along with moderately higher operating costs. We forecast a group EBIT of KWD 27.3 Mn for 2020E, and KWD 64.8 Mn and KWD 66.2 Mn for 2021E and 2022E, respectively.

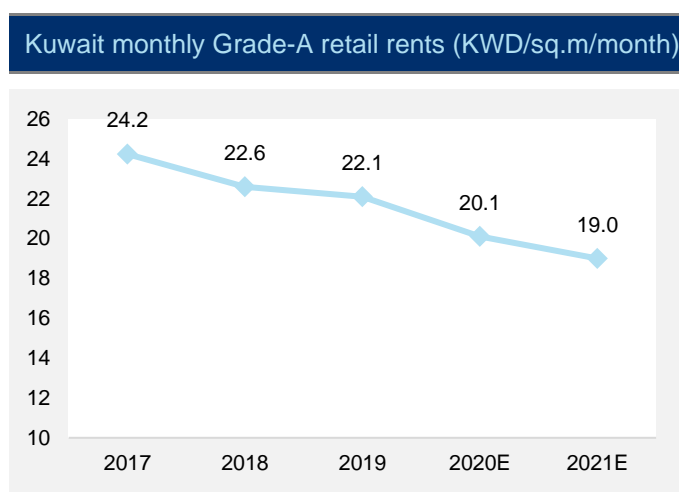
E-tailing accelerates, but brick-and-mortar retail apocalypse fears overdone

In our report- [GCC RE Update - Déjà vu or Different this time?](#), we highlighted that sales via ecommerce channels for certain large retailers in the region had increased 3x-4x from the onset of Covid. This in our view could also lead to some retailers deferring new store openings as well. We believe the current headwinds in the retail sector, and a drop in consumer spending due to an extension of Covid, could lead to lower brick-and-mortar footfalls and sales conversions, and put significant downward pressure on the outlook of retail rents going forward.

For Kuwait, real estate consultant REMI forecasts Grade-A retail space to grow by 18.8% from 814,200 sq.m in 2020 to 967,500 sq.m in 2021E, with significant additions from Assima (GLA: 78,407 sq.m) and Tamdeen Outlet Mall (GLA: 74,834 sq.m). They continue to expect demand for retail mall spaces to be more weaker, and forecast a 5.5% drop in average retail rents for Grade-A spaces from KWD 20.1/sq.m per month in 2020, to KWD 19.0/sq.m per month in 2021E. Nevertheless, REMI expects the lower average rents to help in keeping occupancy rates healthy at 92% in 2021E for Grade-A spaces, up from 90% in 2019, as the market remains largely price sensitive.

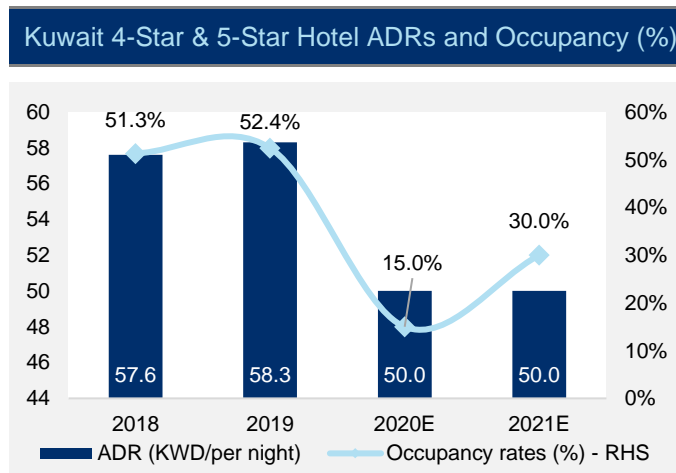


Source: REMI

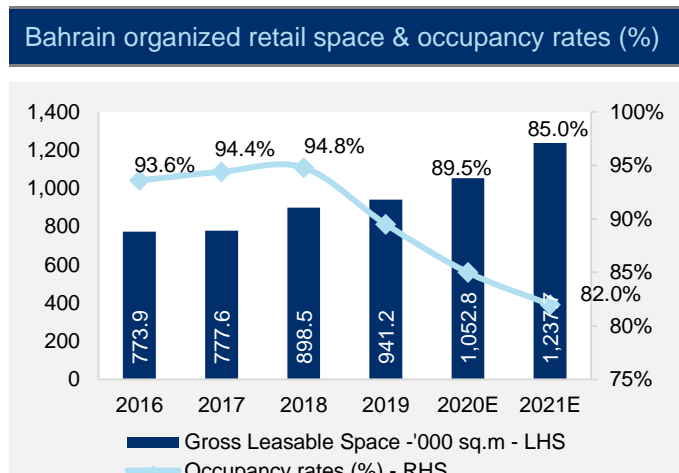


Source: REMI

We however believe that market fears of the 'brick-and-mortar' retail model completely going out of favor are still too aggressive, especially in a GCC context. Further post Covid, we continue to expect Entertainment and F&B tenants to drive incremental demand for mall spaces within the region and in Kuwait, as against demand from retail tenants. This trend should continue in our view, given the limited number of entertainment alternatives available to residents in the GCC.



Source: REMI



Source: REMI

For hotels, REMI forecasts average ADRs for 4-Star and 5-Star to decline around 14% y-o-y to KWD 50/night, as occupancy rates plunge from 52.4% in 2019 to 15% in 2020E. They further expect occupancy rates to recover to 30% in 2021E, but forecast ADRs to remain at KWD 50/night. Although, our ADR and occupancy assumptions for full potential estimates in 2022E represent a jump from

industry forecasts in 2021E, we prefer to alter our forecasts closer to 2022E, once the probable impact of Covid becomes clearer, and based on our discussions with the management going forward.

For Bahrain, REMI expects occupancy rates for organized retail average to fall from above 94% in 2019 to 85% in 2021E, as supply jumps by 31.5% from around 941,000 sq.m in 2019 to 1,237,700 sq.m in 2021. They further expect average lease rates to fall by 9.8% over the period from BHD 9.02/sq.m per month in 2019 to BHD 8.14/sq.m per month in 2020. Bahrain's retail sector demand has been significantly impacted by the onset of Covid as well, that has in turn led to a reduced the number of tourists from Saudi Arabia entering Bahrain via the King Fahd Causeway. Moreover, tourists are now required to follow more stringent protocols, like PCR tests done for each trip, and bear additional costs (BHD 50-60 per trip) associated with the tests. This should deter frequent visits from tourists taking the King Fahd Causeway, until the impact of Covid dissipates, and in turn reduce footfalls into malls in Bahrain in our view.

Ramping up existing operations significant for future capex outlay

Mabaneer announced in mid-Aug 2020 that they have decided to restudy their Avenues Riyadh project in the light of current economic circumstances. In Q4-2019, Mabaneer had guided that a MoU was signed with Nesma & Partners to design and construct Phase I of the project, with a budget of SAR 6.150 Bn and that SAR 5.6 Bn have been secured through an initial agreement with 9 GCC banks. We view this decision constructively, given the significant change in business environment with the onset of Covid, and size of the project, which includes a mall space GLA of 400,000 sq.m & 4 multi-purpose towers. Moreover, Mabaneer mentioned in their H1-2020 conference call that the Avenues Sharjah Project is being re-evaluated, while feasibility studies are being conducted for the Salmiya Project in order to ascertain the best use for the property that would maximize project returns.

Mabaneer under development and upcoming projects

Project	Project Type	Latest Project Description	Status	Included/Not Included in Kamco Invest Forecasts
Avenues Kuwait - Waldorf Astoria	Hospitality	5-Star hotel of 200 keys with expected completion by Q1-2021	Ongoing	Included
Avenues Bahrain Phase II	Retail	Mall GLA of ~50,000 sq.m	Ongoing	Included
Avenues Bahrain Phase II -Hotel	Hospitality	Hotel with 210 keys with expected completion by end 2020/early Q1-2020	Ongoing	Included
Avenues Riyadh	Mixed-Use	Mall GLA of 400,000 sq.m and 4 multi-purpose towers	Under Review	Not Included
Avenues Khobar	Mixed-Use	Mixed-use project over 209,000 sq.m of land space mall space, 4 multi-purpose towers with residential, commercial office, hospitality & medical components	Design	Not Included
Jaber Al Ahmad: J3 - Kuwait	Mixed-Use	PAHW project with retail GLA of 104,000 sq.m and 276 residential units	Construction start date to be finalized	Not Included
Salmiya Project - Kuwait	To be decided	Comprehensive concept and feasibility study for land space of 9,761 sq.m on the Arabian Gulf Street in Salmiya	Under Study	Not included
Avenues Sharjah	Retail	Investment & development of 58,000 sq.m of mall GLA on the Sheikh Zayed Road	Under Review	Not included

Sources: Mabaneer, Kamco Invest Research

In our model forecasts and valuation, in terms of ongoing and upcoming projects, we currently include: 1) 5-Star hotel at Avenues Kuwait – Waldorf Astoria, 2) Avenues Bahrain – Phase II of GLA ~50,000 sq.m and 3) Avenues Bahrain Phase II – Hotel of 210 keys. The Jaber Al Ahmed J3 project with a total project value of KWD 156.3 Mn, in which Mabaneer is the lead developer of the consortium with a 35% participation stake, is expected to be developed over 4 years. Project components include 276 residential units, and a retail component with GLA of 104,000 sq.m. We expect to include this project in our forecasts once a firm construction date is made public. We remain positive on Mabaneer's capital allocation track record thus far, given their ability to put high quality assets in the market and derive high margins from those existing projects. Nevertheless, prior to that, the ramp up of operations at Phase IV and the hotels at Avenues-Kuwait, along with successful completion of ongoing projects in Bahrain are crucial, especially from a cashflow perspective, given the size of planned future projects. We prefer to see more visibility for Mabaneer's capex growth-runway of other regional projects, Kuwait partnerships, and their Salmiya project before including them in our forecasts and valuation.

Mabane Financial Forecasts

Covid impacts Kuwait operations; drives lower EPS for 2020E and 2021E

Our detailed financial forecasts for Mabane over 2020E and 2021E factor in the loss of revenues from the impact of Covid and related shutdowns in 2020E for all operations components, slower ramp-up of Phase IV revenue generation, lower blended rents for Phase I-IV over 2020E-2022E. Forecasts also incorporate delays in the start date of 5-Star Waldorf Astoria, and the impact of Covid-19 on occupancy rates, and ADRs of 4-Star Hilton Garden Inn.

2020 & 2021 Forecasts – Kamco Invest Research						
New vs. Old	2020E			2021E		
Mabane	New	Old	Δ (%)	New	Old	Δ (%)
Revenues (KWD Mn)	64.1	106.3	-40%	105.0	109.9	-4%
GP Margins (%)	64.4%	75.5%	-15%	75.1%	73.6%	2%
EBIT (KWD Mn)	27.3	69.0	-60%	64.8	69.4	-7%
Net Income (KWD Mn)	22.2	64.6	-66%	57.8	65.4	-11%
EPS (KWD)	0.020	0.062	-68%	0.052	0.063	-17%
Net Debt (KWD Mn)	295.4	228.5	29%	247.8	171.2	45%

Source: Kamco Invest Research

Our forecasts only include Avenues Kuwait projects and hotels (including the under construction 5-Star Waldorf Astoria), along with existing and ongoing projects in Bahrain. As a result, we forecast EPS estimates of KWD 0.020/share for 2020E and AED 0.052/share for 2021E.

Mabane Financials						
Balance Sheet (KWD Mn)	2017	2018	2019	2020E	2021E	2022E
Assets						
Cash and cash equivalents	14.5	18.4	72.6	64.4	121.0	155.8
Receivables	43.1	28.8	19.8	21.7	22.1	22.5
Total current assets	57.6	47.2	92.4	86.1	143.0	178.3
Net property, plant and equipment	3.5	3.4	4.6	122.1	123.3	124.3
Other assets	742.3	812.2	868.1	775.9	780.2	780.9
Total assets	803.5	862.8	965.1	984.1	1,046.6	1,083.4
Liabilities						
Total debt	288.6	303.3	340.6	359.7	368.7	361.4
Accounts payable and other liabilities	131.0	134.2	151.5	136.2	137.3	138.9
Total liabilities	419.6	437.5	492.0	495.9	506.1	500.3
Shareholders' Equity						
Share capital	110.2	114.9	120.8	127.0	127.0	127.0
Retained earnings	179.9	207.2	234.0	240.7	293.0	335.7
Other equity	93.7	103.1	118.3	120.5	120.5	120.5
Total Equity	383.8	425.2	473.1	488.2	540.5	583.2
Total Liabilities and Equity	803.5	862.8	965.1	984.1	1,046.6	1,083.4
Income Statement (KWD Mn)	2017	2018	2019	2020E	2021E	2022E
Revenue	77.2	85.4	96.4	64.1	105.0	107.5
Cost of goods sold	-16.9	-17.8	-22.1	-22.8	-26.1	-27.2
Gross profit	60.4	67.6	74.2	41.3	78.9	80.4
General and administrative expenses	-1.8	-2.4	-2.0	-2.7	-2.7	-2.7
EBITDA	58.5	65.2	72.2	38.6	76.2	77.6
Depreciation and amortization	-7.0	-8.7	-10.1	-11.3	-11.3	-11.4
EBIT	51.5	56.5	62.2	27.3	64.8	66.2
Finance costs	-0.3	-2.4	-4.0	-5.3	-5.5	-5.5
Other Income/Loss	0.1	0.7	1.2	1.5	1.5	1.6
Net profit before taxes	51.3	54.7	59.3	23.5	60.9	62.4
Provision for Income Taxes	-2.5	-2.6	-3.2	-1.6	-3.3	-3.4
Net profit after taxes	48.9	52.1	56.1	21.9	57.6	59.0
Minority interest	0.3	0.4	0.3	0.3	0.3	0.3
Net profit attributable to parent	49.2	52.5	56.4	22.2	57.8	59.2
EPS (KWD)	0.044	0.048	0.051	0.020	0.052	0.054
Cash Flow (KWD Mn)	2017	2018	2019	2020E	2021E	2022E
Net cash from operating activities	102.1	54.6	89.1	34.0	72.8	74.8
Net cash (used in) from investing activities	-93.4	-44.7	-43.5	-36.0	-14.7	-11.2
Net cash from (used in) financing activities	-8.4	-6.1	8.5	-6.2	-1.4	-28.9
Change in cash and cash equivalents	0.3	3.9	54.2	-8.2	56.6	34.8
Cash at the end of the year	14.5	18.4	72.6	64.4	121.0	155.8

Source : Kamco Invest Research and Mabane

Valuation & Financial Ratios						
Key Ratios	2017	2018	2019	2020E	2021E	2022E
Asset Structure and Leverage Ratios						
Profitability Ratios						
Return on Average Assets (%)	6.4%	6.3%	6.2%	2.3%	5.7%	5.6%
Return on Average Equity (%)	13.5%	13.0%	12.6%	4.6%	11.2%	10.5%
ROIC (%)	8.6%	8.6%	9.0%	3.4%	7.8%	7.9%
Margins						
Gross profit margin (%)	78.2%	79.1%	77.0%	64.4%	75.1%	74.7%
EBITDA margin (%)	75.8%	76.3%	75.0%	60.2%	72.5%	72.2%
EBIT margin (%)	66.8%	66.1%	64.5%	42.6%	61.7%	61.6%
Net profit margin (%)	63.6%	61.5%	58.5%	34.6%	55.1%	55.1%
Per Share Data and Valuation Ratios						
Earnings Per Share (KWD)	0.050	0.050	0.051	0.020	0.052	0.054
Book Value Per Share (KWD)	0.35	0.38	0.43	0.44	0.49	0.53
Dividend Per Share (KWD)	0.01	0.01	0.01	0.01	0.02	0.02
PE (x)	12.0	10.7	16.7	37.5	14.4	14.0
PB (x)	1.7	1.4	2.0	1.7	1.5	1.4
Dividend Yield (%)	2.1%	1.7%	1.1%	0.7%	2.0%	2.0%

Source : Kamco Invest Research and Mabanee

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- * **Outperform:** Target Price represents expected returns $\geq 10\%$ in the next 12 months
- * **Neutral:** Target Price represents expected returns between -10% and $+10\%$ in the next 12 months
- * **Underperform:** Target Price represents an expected return of $< -10\%$ in the next 12 months

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Kamco Investment Company - K.S.C. (Public)

Al-Shaheed Tower, Khalid Bin Al-Waleed Street- Sharq

P.O. BOX : 28873, Safat 13149, State of Kuwait

Tel: (+965) 2233 6600 Fax: (+965) 2249 2395

Email : kamcoird@kamcoinvest.com

Website : www.kamcoinvest.com