MANAGEMENT DISCUSSION AND ANALYSIS REPORT

Description of the Company and Business

Muscat City Desalination Company S.A.O.G. (hereinafter referred to as **MCDC** or the **Company**) was incorporated as an S.A.O.C. with the commercial registration number 1163374 for an unlimited duration on 19 January 2013.

The Company underwent an Initial Public Offering (**IPO**) exercise in late 2017 and was subsequently listed on the Muscat Securities Market (**MSM**) on 2 January 2018.

The Company's core business activity is to develop, own and operate the Al Ghubrah Independent Water Plant, a Sea Water Reverse Osmosis (**SWRO**) desalination plant, with a contracted capacity of 191,000 cubic meter per day (42 Million Imperial Gallons per Day), located in North Ghubrah, Muscat Governorate, Sultanate of Oman (**Plant**). The Plant has been in commercial operations since 19 February 2016.

The Company generates its revenues from the sale of desalinated water pursuant to a Water Purchase Agreement (**WPA**) with the Oman Power and Water Procurement Company (**OPWP)**. The desalinated water from the Plant is fully contracted to OPWP to meet the growing water demand of the Interconnected Zone (Northern Region of Oman) during the term of the WPA. The contracted water capacity of the Plant represents approximately 20% of the operating capacity in the Interconnected Zone in accordance with OPWP's 7-year statement (2018-2024).

The potable water is delivered to the Public Authority for Water (**PAW**) reservoirs located adjacent to the Plant.

Electricity is supplied to the Plant by Muscat Electricity Distribution Company (**MEDC**) pursuant to an Electricity Supply Agreement (**ESA**). The Company as System User, has entered into the Electricity Connection Agreement (**ECA**) with Oman Electricity Transmission Company (**OETC**) to secure connection to the Transmission System over the contracted WPA period.

Competitive Strengths

The Company's competitive strengths include the following:

- One of the largest operating SWRO desalination plant at a single location in Oman.
- Well-established contractual framework with long term WPA, ensuring cash flow protection against adverse events such as buyer risk events and force majeure.
- Stable and predictable cash flows, resilient to potential shocks in electricity prices and water demand during the term of the WPA.
- Proven, long-term and reliable SWRO desalination technology.
- Experienced Project Founders with an established track record being able to transfer skills and know-how.
- Fully operational Plant operated by experienced and skilled personnel complying fully with the highest levels of Omanisation requirements.

Contractual Framework

MCDC's contractual framework is as shown below.

Water Purchase Agreement

The WPA was executed between the Company and OPWP on 11 February 2013. The WPA details the commercial terms agreed between the Company and OPWP and sets out standard representations and warranties that the Company is required to provide.

The WPA sets out a number of obligations of the Company throughout the tenure of the agreement. Among other things, the Company must, acting as a reasonable and prudent operator, operate and maintain the Plant in such manner so as to ensure that the Plant is capable of operating and maintaining water production on a continuous and reliable basis.

Under the WPA, the Company is also obliged to exclusively sell water output to OPWP and in return, receives from OPWP, payment for Water Capacity Charges and Water Output Charges. The Water Capacity Charges are designed to cover fixed costs such as debt service, return on capital, tax payments as well as fixed costs to operate and maintain the Plant (such as manpower, spare parts, maintenance and insurance). The Water Output Charges compensates the Company for variable operation and maintenance costs (such as chemicals, SWRO membranes, cartridge filters, consumables, spare parts) and the electricity charges for the water output delivered.

Electricity charges are calculated on the contracted specific power consumption of the Plant.

The Water Capacity Charges are also adjusted for scheduled unavailability, forced outages, derating of the Plant and also to take into consideration inflation and exchange rate movements. The Water Output Charges are adjusted for changes in the exchange rate, US Producer Price Index (US PPI) and the Omani CPI.

The WPA also outlines various buyer risk events and the relief that the Company will receive should certain specified events occur that will hinder the Company from performing its obligations under the WPA. If a relevant buyer risk event is established in accordance with the terms set out in the WPA, the Company will not be liable for any failure to perform or any delay in its performance and will continue to be entitled to be paid capacity charges during the relevant period in accordance with the terms of the WPA. In the event that it is determined that a material adverse change has occurred and such material adverse change was caused by a buyer risk event or events which constitute a material adverse change, OPWP shall propose a mechanism to the Company in order to adjust the Water Capacity Charges and/or the Water Output Charges, as appropriate, or reimburse the Company by an agreed reimbursement mechanism.

The WPA also provides for relief to the Company if various force majeure events hinder the Company from performing its obligations under the WPA. If it can be established that a force majeure event has occurred, or will occur, and that it could not have been mitigated by the Company, acting as a reasonable and prudent operator, the Company will be relieved from liability for any failure to perform its obligations under the WPA for the duration of the force majeure event and the term of the WPA will be extended by the period for which the force majeure event hindered the Company from performing its obligations. Furthermore, the Company shall be entitled to continued receipt of capacity charges to the extent of its availability during the force majeure period.

Subject to certain force majeure, buyer risk events and termination provisions contained therein, the term of the WPA which commenced on 11 February 2013 shall expire on 11 October 2034.

Electricity Supply Agreement (ESA)

The ESA was entered into between MEDC and the Company on 11 February 2013 for the supply of electricity up to a maximum of 40MVA in accordance with the Permitted Tariffs in the ESA for operating the Plant. Both MEDC and the Company have the right to terminate the ESA by giving at least thirty days prior written notice to the other party.

Electricity Connection Agreement (ECA)

The ECA was entered into between the Company and OETC, a wholly owned Government company established in 2003, on 11 February 2013. The ECA sets out the terms and conditions for the connection to the Transmission System. It establishes a framework to provide for, amongst others:

i. the payment by the Company to OETC of the connection fee; and

ii. enforcement of the Grid Code between OETC and the Company.

The ECA became effective from the date of its execution and shall remain in force for an initial period of 25 years (**Initial Term**) and will continue in force beyond the expiry of the Initial Term unless and until either party terminates the ECA on six months prior notice to the other, provided that no such notice, shall take effect before the expiry of the Initial Term.

Usufruct Agreements (UAS)

The UAS was executed between the Ministry of Housing (**MoH**) and the Company on 11 February 2013. The UAS relates to the site on which the Plant is located (**Site**). It has a term of 25 years from the date of ratification of the UAS by the Government, subject to a further extension of 25 years at the option of the Company. The Company is under the obligation to only use the Site for the stated purpose as described in the UAS.

In accordance with the UAS, MoH has provided the Site to the Company free and clear of any right adverse to the usufruct right so granted including, but not limited to, any third party claim that may be made relating to the Site. MoH also ensures that the Company has undisturbed enjoyment of the Site throughout the term of the UAS.

Operations and Maintenance Agreement (O&M Agreement)

The O&M Agreement was entered into between the Company and Muscat City Desalination Operations and Maintenance Company LLC (herein referred to as **MCDOMC** or the **Operator**) on 27 November 2013. It provides for the provision of O&M services by the Operator. The O&M Agreement requires the Operator to operate and maintain the Plant until 11 October 2034, being 20 years after the Scheduled Commercial Operations Date (SCOD) of 11 October 2014.

The terms of the O&M Agreement may be modified to reflect any extension of the term of the WPA as may be determined between the Company and OPWP in accordance with the terms of the WPA. The O&M Agreement was amended on 21 October 2017 to revise the water capacity O&M charge due to the non-requirement of the second pass Reverse Osmosis sub-system of the Plant and to provide clarity on the sharing of the savings on the electricity consumption charges with the Operator.

Under the O&M Agreement, the Operator is responsible, amongst others, for:

- operating the Plant during the operation period in accordance with the scheduling requirements and the dispatch instructions issued to the Company by OPWP from time to time;
- maintaining the Plant to ensure that the Plant operates at the requisite capacity;
- recruiting, employing and training sufficient staff to operate and maintain the Plant;
- programming and carrying out such performance tests as may be required by the Company or OPWP from time to time and any additional performance tests as the Company or OPWP may propose in accordance with the testing procedures and restrictions under the WPA;
- performing all operation and maintenance works and procure all resources and materials to comply with the Omanisation Plan specified in the O&M Agreement;
- satisfying all of the Company's operation and maintenance related obligations under the Project Agreements;
- affording all reasonable assistance and co-operation in relation to the performance of the Company's obligations under the Project Agreements; and
- not undertaking any action or failing to take any action which would cause the Company to be in breach of any of its obligations under the Project Agreements.

The fees payable under the O&M Agreement consist of fixed and variable components.

EPC Contract

The EPC Contract was executed between the Company and International Water Treatment Company (**IWT**) on 10 April 2013. It established the terms upon which IWT was to design, engineer, manufacture, supply, procure, transport, erect, construct, install, test and commission the Plant and to warrant such works and remedy any defects or non-compliances therein.

In consideration of these works, the Company was to pay IWT the contract price in accordance with the milestone payment schedule.

The EPC Contract sets out the obligations of IWT. Amongst others, IWT was to ensure that the works and materials used in the construction were free from charges or liens and defects in title, design or workmanship and that the works would meet all environmental requirements and all applicable laws. IWT was obliged to attain Taking Over of the Plant on or before the Time for Completion, matching the Scheduled Commercial Operations Date (**SCOD**). The EPC Contract contains provisions for warranties as well as punch list items of the Works (as defined under the EPC Contract) noted by the Company as requiring rectification by IWT within twenty-four months from Taking Over date. The Taking Over date was 19 February 2016.

If the Contractor repairs, replace or renews all or any part of the Plant or works, then the Defects Liability Period shall apply to the part of the Plant or the Works so repaired, replaced or renewed until the expiration of 24 months from the date of such repair, replacement or renewal, provided that the defects liability period shall not be greater than 48 months from Taking Over Date. As a result, IWT was responsible for carrying out at its cost all works of redesign, repair, reconstruction, rectification, renewal and replacement for the purpose of making good of Defects (as defined under the EPC Contract) or damage to the Plant or any part of the Works which might appear as a result of a Defect and for which IWT was responsible pursuant to the terms of the EPC Contract. During the defects liability period, a total of 133 warranty items had been raised, which have all been closed or commercially settled with the EPC Contractor in 2020.

Risk Management

MCDC affirms its commitment towards ensuring and maintaining a sound internal control system which encompasses good governance, risk management and control processes. In light of this, the Company confirms that there is a proper risk management assurance process in place to identify, evaluate and manage significant risks impacting the Company's achievement of its objectives. The Company also acknowledges the presence of a sound system of internal control in safeguarding shareholders' investments, the Company's assets and other stakeholders' interests as well as ensuring compliance with applicable laws and regulations.

MCDC's risk management objectives are:

- Creating the right awareness and understanding of risk at all levels of the organisation.
- Instilling a culture of risk management and risk ownership as everyone's responsibility.
- Identifying risks and managing them well within the risk appetite of the organisation.
- Embedding risk management in the way the business is run.
- Developing a common risk language.
- Complying with appropriate risk management practises in terms of corporate governance guidelines.

Financial Arrangement

The Company has entered into financing agreements with a consortium of international banks, for an aggregate amount of OMR 81.25 million (US$211.30 million). Senior debts are hedged in compliance with the requirement of the financing agreements via interest rate swap agreements. This further improves the predictability of cashflows of the Company.

Operation and Maintenance

The Plant is operated and maintained during the term of the WPA by the Operator, through the O&M Agreement with the Company. The Operator is primarily responsible for the Plant's availability and efficiency, meeting dispatch instructions, operational cost control and most importantly, the Health, Safety & Environment (HSE) compliance. The Operator is also responsible for ensuring adequate spare parts are available and that its employees are properly qualified and trained.

The maintenance of the Plant was undertaken in accordance with the Original Equipment Manufacturer (OEM) recommendations and in accordance with the O&M manuals. The maintenance schedule is maintained in the Computerized Maintenance Management System (CMMS).

Corporate Governance

The Board of Directors and Management of the Company and the Operator are committed in ensuring that the highest standards of corporate governance are practiced in the Company and the Operator. This is practiced, as a fundamental part of their respective responsibilities in managing the businesses and affairs, protecting and enhancing stakeholders' values as well as financial performance while promoting the highest standards of integrity, transparency and accountability.

Discussion on Operational Highlights and Financial Performance

Health, Safety and Environment (HSE)

The HSE Policy commits the Company and the Operator in creating a safe, secure and healthy working environment and the elimination of all work-related incidents and injuries. The Company and its Operator have HSE policies in place to conduct all operations in a manner that protects the HSE of employees, sub-contractors and the public while complying with all applicable legal and other requirements.

All employees and contractors are required to perform their work in accordance with the implemented HSE policy, which is carried out through the following practices:

- communicating the HSE policy to all interested parties;
- providing the necessary resources to prevent ill health and injury of all working personal and to minimize pollution and environmental impact associated with activities;
- ensuring employees and contractors are provided with adequate training and supervision for the safe performance of the work;
- making all employees and contractors responsible and accountable for health, safety and environment in their daily work activities;
- establishing, maintaining, rehearsing and reviewing with concerned groups all emergency response plans to prevent injury and accidental environmental impact while minimising any damage to company property and the community; and
- seeking continual improvement in HSE performance through periodic monitoring and reviewing of policy, objective and targets.

During the year, there were neither Lost Time Incidents (**LTI**) nor environmental incidents. As at 31 December 2020, the Company achieved 1768 days without an LTI since its Commercial Operations Date (**COD**) on 19 February 2016. The total man-hours is 59,229 hours.

The Operator had, in April 2017, been awarded ISO 14001:2004 Environmental Management System and OHSAS 18001:2007 Occupational Health and Safety Management System certification. In September 2018 the ISO 14001:2004 had been successfully migrated to ISO 14001:2015.

In addition to the above measures, the Company and the Operator have developed and implemented the following procedures to prevent employees, subcontractors on site and visitors from the infection of COVID-19, thereby providing a safe and healthy work environment and ensuring the total availability of the Plant and its drinking water production.

- Temperature screening at the Plant entrance;

- Replacing face-to-face meetings with conference calls;
- Enforcement of facial mask usage in the Plant;
- Installation and distribution of sanitizers;
- Routine disinfection of meeting rooms and work stations;
- Installation of informative posters in the buildings;
- Splitting of teams (maintenance, operation and laboratory) to work in shifts to minimize interactions between employees.

Capacity

The capacity of the Plant is defined by the total capacity of water (m^3/day or MIGD) which can be delivered by the plant into the PAW water transmission system.

The contracted capacity of the Al Ghubrah Independent Water Plant under the WPA is 42 MIGD applicable from April 2020 to March 2021, following the Annual Performance Tests conducted in March 2020 which demonstrated that the plant met the contractual requirements under the WPA.

Plant Availability & Output

The reliability of the Plant is a measure of its availability to deliver the declared capacity in accordance with the WPA. For the financial year 2020, the Company achieved a higher availability of 95.00% after scheduled and forced outages compared to 93.84% in 2019.

During the year, the Plant experienced negligible amount of algae bloom, and the limited impact of the algae bloom on the operations and availability of the Plant was adequately controlled with the incorporation of the Dissolved Air Flotation (**DAF**) system adopted at the Plant.

However, the Plant experienced a series of jelly fish infestation in March, April, and June of 2020. The jelly fish infestation, which drifted with the sea currents, clogged the sea water intake screens and reduced the amount of seawater into the intake pipes. This reduction of sea water intake directly affects the amount of potable water produced by the Plant, thus causing the forced outages.

In addition, in December 2020, the Company implemented the major maintenance, called "pigging". The pigging was intended for the purpose of cleaning-up its one of two seawater intake pipes to remove massive volumes of marine growth such as barnacles, mussels and other species of adhesive shellfish that have grown and adhered for years to the inside wall of its intake pipes, which restricted the amount of seawater into the intake pipes and reduced the efficiency of the plant. The pigging was, after series of preparation works throughout the year, executed in December 2020, and this successfully removed tremendous amounts of marine growth from the intake pipe thereby improving the Plant's overall efficiency. However, the unexpected massive volume of marine growth (or debris) blocked the outlet of the intake pipe, which eventually caused forced outages. Despite it, after the implementation of the pigging, the plant successfully demonstrated immediate effects to improve its efficiency. The Company plans to implement the pigging again for the remaining seawater intake pipe in 2021, which is expected to further improve the Plant's performance.

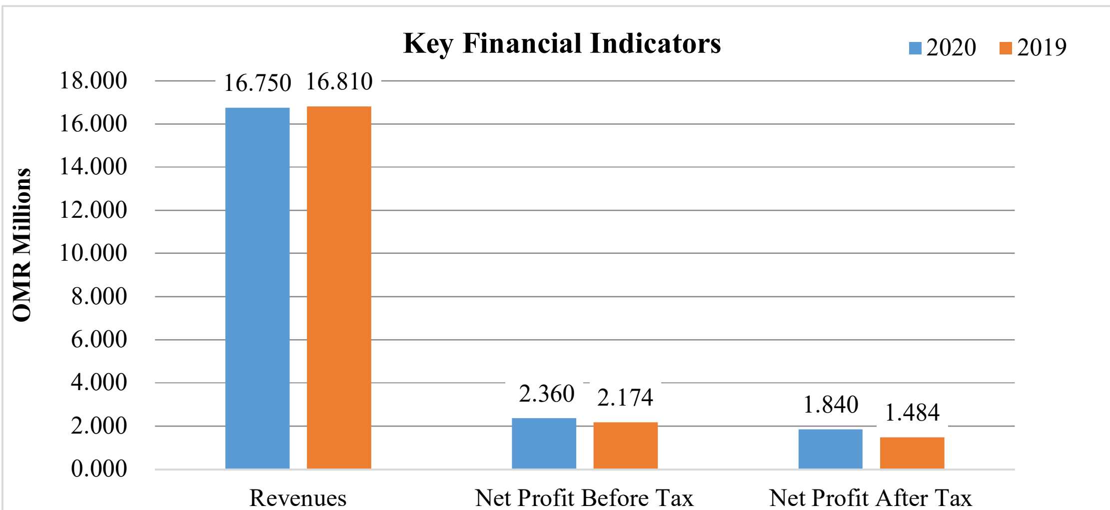
Overall, total forced outages in 2020 was 1.36% against 1.09% for 2019.

Notwithstanding the above, during FY2020, the Plant produced a total of 64,845,538 m^3/day of potable water with a utilization factor averaging 92.80% of total plant capacity or 96.36% of scheduled available capacity. Plant production is determined by the daily dispatch instruction issued by PAW.

Financial Highlights

All figures in OMR million		2020	2019
Revenues	1	16.750	16.810
Net Profit	2	1.840	1.484
Net Profit before Finance Costs	3	4.797	4.627
Total Assets	4	94.004	93.524
Capital (Paid-up)	5	15.555	15.555
Shareholder's Fund (Net Assets)	6	13.629	14.445
Term Loan (*1)	7	57.532	60.719
Weighted average number of shares	8	155,550,400	155,550,400
Actual number of shares outstanding	9	155,550,400	155,550,400
Ordinary dividends	10	-	1.253

(*1) Excluding unamortized transaction costs



Key Financial Indicators		2020	2019
Net Profit Margin	= 2/1	10.99%	8.83%
Return on Capital (Paid-up)	= 2/5	11.83%	9.54%
Return on Capital Employed	= 3/(6+7)	6.74%	6.16%
Debt Equity Ratio	= 7 : 6	81 : 19	81 : 19
Net assets per share (RO)	= 6/8	0.088	0.093
Basic Earnings Per Share (RO)	= 2/8	0.012	0.010
Dividend per share (Baiza)	= 10/9	-	8.0550

Analysis of Profit and Loss

The Company managed to generate operating revenue of OMR 16.750 million in FY2020, 0.4% lower than the OMR16.810 million in FY2019. This decrease is mainly due to higher unscheduled outage rate in FY2020.

The profit before tax for FY2020 was OMR 2.360 million, higher compared with OMR 2.174 million in FY2019. The net profit after tax was also higher in FY2020 OMR 1.840 million compared with OMR 1.484 million in FY2019.

Analysis of Balance Sheet

Total assets of the Company stood at OMR 94.004 million as at 31 December 2020 compared with OMR 93.524 million in FY2019. The increase in the total assets was mainly due to higher cash position in FY2020 as compared to FY2019.

The cash and cash equivalents as at 31 December 2020 was OMR 4.209 million compared with OMR 1.973 million as at 31 December 2019.

The shareholders' funds as at 31 December 2020 was OMR13.629 million compared with OMR14.445 million as at 31 December 2019. The decrease in the shareholders' funds was mainly contributed by the higher negative changes in the Hedging Reserve in FY2020 as compared to FY2019. The negative Hedging Reserve (net of deferred tax) has increased by OMR 2.656 million in FY2020 from OMR 3.223 million in FY2019, reflecting the fair value of the 2 interest rate swap arrangements as at the balance sheet date. This has affected the Company's capability to distribute dividends to its shareholders in FY2020.

Term loans (including non-current and current balances) reduced to OMR 57.532 million as a result of scheduled repayments made in accordance with finance agreements.

The Company continues to make adequate provision for asset retirement obligations to fulfil its legal responsibilities to remove the Plant at the end of its useful life and restore the land to its original state, prior to handing over.

Dividend Distribution

Despite a higher net profit in 2020, the Company has however, been unable to declare or pay any dividend in 2020 in line with the guidance provided by the Capital Market Authority based on Article 130(3) of the new Commercial Companies Law, promulgated pursuant to SD 18/2019 (**CCL**). Whilst the Company's audited financial statements for 2020 demonstrate that it has recorded a net profit of OMR 1.84 million after taxation, the Company sustains a loss in other comprehensive income of OMR 2.65 million due to changes in fair values of derivative financial instruments, which is featured as cumulative net change in the fair value of cash flow hedging instruments of OMR 5.88 million in its balance sheet and has resulted in the erosion of the total equity of OMR 13.63 million against the share capital of OMR 15.55 million. The loss in other comprehensive income, which is unrealized, is a direct result from the lower interest rates in the current market. Even though, such erosion in equity does not affect the Company's cash flow position, the Company has been advised that it cannot distribute dividends unless such erosion has been fully extinguished referring to the Article 130(3) of the CCL. The Company has been exploring possibilities to distribute dividends to its shareholders in a way which is fully compliant with the CCL and other applicable Omani legislation with utmost efforts.

Employees, Training and Omanisation

MCDC and its Operator takes Omanisation as a responsibility to assist in the building of Omani expertise in the water desalination sector. Together, the Company and its Operator employ a total of 50 employees, of which 37 employees are Omani citizens.

Training is conducted frequently, with strong emphasis on HSE, operational improvements and personal development. The employees are encouraged to attend the continuous education programmes and seminars from time to time to keep themselves abreast with the latest developments as well as to further enhance their competency and professionalism in discharging their duties.

The Project had achieved an overall Omanisation ratio of 74% as at 31 December 2020.

Internal control systems

The Board acknowledges that ensuring sound Internal Control Systems requires effective interaction among the Board, Management and its auditors. The Board, in ensuring effective discharge of its responsibilities, and is assisted by the Board Committees, namely the Audit Committee and, Nomination and Remuneration Committee. Each committee has clearly defined terms of reference.

MCDC also has a comprehensive system of internal controls in place, comprising a well-defined governance structure, clearly outlined delegated levels of authority, annual budgets and plans to deliver the Company's strategy, supported by regular reporting of these plans and budgets to the Board of Directors.

Outlook

The Company will endeavor to ensure that it continues to take reasonable and prudent measures to improve its performance for FY2021, by improving the Plant's reliability and availability, without compromising on HSE matters.