

Gulf International Services (GISS)

Recommendation	ACCUMULATE	Risk Rating	R-4
Share Price	QR1.914	Current Target Price	QR2.100
Implied Upside	9.7%	Old Target Price	QR1.800

Profitability to Resurface in 2H2021; Raising Price Target

We are updating our estimates and increasing our price target on GISS. GISS reported a slight bottom-line loss for 1H2021 and we expect 2H2021 results to improve considerably. This should be driven by its drilling segment. GISS' drilling business, which was upended by coronavirus-related restrictions leading to rig suspensions, seems to be turning the corner. Given the strength in oil prices, we expect new higher offshore rates (indexed to oil prices) to kick in from July 2021 for all seven offshore rigs. Moreover, on the onshore side, four out of seven rigs were idle in 1H2021 but two have already started operating with the remaining two slated to come back into service in 4Q2021 and early 2022. Finally 3Q2021 should be the first quarter of full contribution from all five offshore rigs being deployed under the GulfDrill JV for the NFE project (remaining 3 rigs started in 2Q2021). So net-net, we do envision an acceleration in momentum in the drilling segment in 2H2021 and onward. We expect earnings to surface back into the green (ex. any one-offs, such as impairments) for FY2021 as drilling loss declines significantly. Other segments also contribute positively, while continued progress in costs reduction and lower finance charges help boost earnings. We roll our DCF-based model forward to 2022 and increase our price target from QR1.800 to QR2.100. Our rating remains at Accumulate.

Highlights

- GISS faced a subdued 1H2021; expectations are decidedly buoyant for 2H2021, however. The company posted a loss of QR0.8mn in 1H2021 vs. a profit of QR54.0mn in 1H2020. Consistent with their 1Q2021 commentary, management continued to point to a recovery in the oil & gas sector in 2Q2021. However, they maintained that positive signs of recovery remained uneven within the group's operating segments – aviation/insurance were improving with drilling remained moribund given rig suspensions/depressed day rates. For more details about the company's 1H2021 results, please see our earnings update [report](#). Going forward, given the uptick in drilling segment fundamentals mentioned previously, we expect earnings to swing back into the green in 2H2021. We now expect 2H2021 earnings to come in at QR65.2mn but could revise our estimates after GISS reports its 3Q2021 results. We do note that given the company's low level of earnings along with paper-thin net margins, quarterly earnings could be subject to significant volatility.
- We expect a more than doubling in net income in 2022 to QR135.5mn. Around 56% of the earnings growth should be driven by drilling and 37% should be propelled by the aviation segment. We note GISS' insurance business is not currently exposed to the retail health insurance segment. However, Al Koot is conducting a feasibility study to consider targeting this segment to take advantage of the mandatory health insurance requirement for expats/visitors expected in place within six months ahead of the FIFA World Cup Qatar 2022. This could add to further earnings upside. We also do not expect significant growth from the catering segment (Amwaj), which could create an upside risk to estimates if we see further traction due to the World Cup. Finally, continued progress in costs reduction and lower finance charges should help boost earnings.
- The NFE project remains a significant catalyst for future growth in GDI & GISS. The company deployed the remaining three rigs (Java Star, W-Castor and W-Tucana) in its GulfDrill JV in 2Q2021. These five rigs deployed by GDI will undertake an 80-well drilling program for Qatar's North Field East project.

Catalysts

- Positive newsflow/performance on the drilling front and signs of growth in the other segments should help. We stay longer-term positive on GISS shares but the stock remains in a "show-me" mode. Lacking a dividend-related catalyst that generally benefits Qatari companies in 4Q/early 1Q, we expect improving financial performance to drive stock price performance over the next 12 months. Moreover, we continue to believe the progress made in costs reduction thus far should dovetail with an expected recovery in market fundamentals as we move forward. Favorable updates on debt restructuring, which was put on the back burner due to COVID-19, could also please equity investors.

Recommendation, Valuation and Risks

- Recommendation and valuation: We rate GISS an Accumulate with a TP of QR2.100. GISS trades at 2022 & 2023 EV/EBITDA multiples of 9.4x and 7.6x, respectively.
- Risks: Geopolitical risks cannot be modeled. Oil price volatility can hurt operations and debt restructuring efforts. Given the low level of absolute earnings, along with paper-thin net margins, quarterly earnings could be subject to significant volatility. Debt levels are high (2020: QR4.4bn/6.7x net-debt-to-EBITDA) but manageable in light of 1.3x interest coverage (2021e) and GISS' attempts to restructure/refinance its leverage going forward. Further decline in rig rates/utilizations could pressure shares. GISS also faces concentration risk given its exposure to QP/affiliates.

Key Financial Data and Estimates

	2020	2021e	2022e	2023e
EPS (QR)	(0.17)	0.03	0.07	0.11
P/E (x)	N/M	55.2	26.3	16.9
EV/EBITDA (x)	11.7	11.6	9.4	7.6

Source: Company data, QNB FS estimates; Note: All data based on current number of shares

Key Data

Bloomberg Ticker	GISS QD
ADR/GDR Ticker	N/A
Reuters Ticker	GISS.QA
ISIN	QA000A0Q6LH4
Sector	Industrials
52wk High/52wk Low (QR)	2.040/1.330
3-m Avg. Volume (mn)	14.8
Mkt. Cap. (\$ bn/QR bn)	1.0/3.6
EV (\$ bn/QR bn)	1.8/6.5
FO Limit* (%)	49.0
Current FO* (%)	10.5
Shares Outstanding (bn)	1.9
1-Year Total Return (%)	22.0
Fiscal Year End	December 31

Source: Bloomberg (as of October 27, 2021), *Qatar Exchange (as of October 27, 2021); Note: FO is foreign ownership

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Key Segment Details

Key Segment Details

In QR mn	2020	2021e	2022e	2023e	2024e
Revenue	2,998	3,042	3,263	3,340	3,396
<i>Gulf Drilling International (GDI)</i>	923	1,004	1,133	1,149	1,152
<i>Gulf Helicopters Company (GHC)</i>	688	698	735	761	784
<i>Amwaj Catering Company (AHC)</i>	406	349	374	384	392
<i>Al Koot Insurance & Reinsurance (AKIR)</i>	981	991	1,021	1,046	1,067
	2020	2021e	2022e	2023e	2024e
Net Income	(319)	64	135	210	254
Net Margin	-11%	2%	4%	6%	7%
<i>Drilling</i>	(453)	(223)	(183)	(128)	(121)
<i>Net Margin</i>	-49%	-22%	-16%	-11%	-10%
<i>Helicopters</i>	383	238	264	278	290
<i>Net Margin</i>	56%	34%	36%	37%	37%
<i>Catering</i>	(10)	(20)	(7)	11	26
<i>Net Margin</i>	-2%	-6%	-2%	3%	7%
<i>Insurance</i>	52	72	84	95	106
<i>Net Margin</i>	5%	7%	8%	9%	10%
	2020	2021e	2022e	2023e	2024e
EBITDA	564	549	641	730	781
EBITDA Margin	19%	18%	20%	22%	23%
<i>Drilling</i>	202	164	202	247	257
<i>EBITDA Margin</i>	22%	16%	18%	21%	22%
<i>Helicopters</i>	476	320	348	364	379
<i>EBITDA Margin</i>	69%	46%	47%	48%	48%
<i>Catering</i>	13	1	15	33	49
<i>EBITDA Margin</i>	3%	0%	4%	9%	12%
<i>Insurance</i>	41	54	65	76	86
<i>EBITDA Margin</i>	4%	5%	6%	7%	8%

Source: Company data, QNB FS estimates

Ratio Analysis

Key Metrics

Particulars	2015	2016	2017	2018	2019	2020	2021	2022	2023
Growth Rates									
Revenue	6.6%	(28.2%)	(19.6%)	4.8%	19.5%	(0.4%)	1.5%	7.3%	2.3%
Gross Profit	1.2%	(56.2%)	(14.9%)	(10.4%)	0.5%	(18.2%)	(21.9%)	29.7%	25.9%
EBITDA	(18.9%)	(40.0%)	(17.6%)	3.5%	(2.9%)	(22.1%)	(2.6%)	16.7%	14.0%
EBIT	(33.4%)	(69.0%)	(21.8%)	10.0%	2.9%	(51.3%)	25.1%	52.6%	33.6%
PAT/EPS	(43.2%)	(91.6%)	26.9%	N/M	N/M	N/M	N/M	110.3%	55.0%
DPS	(81.8%)	0.0%	(100.0%)	N/A	N/A	N/A	N/A	N/A	N/A
CFPS	25.3%	(35.1%)	(24.2%)	(39.7%)	86.9%	(48.5%)	7.6%	32.6%	12.8%
FCFPS	N/M	(59.3%)	32.4%	(41.9%)	222.5%	(57.7%)	9.4%	55.8%	15.2%
Operating Ratios									
Gross Margin	29.1%	17.7%	18.8%	16.0%	13.5%	11.1%	8.5%	10.3%	12.7%
Gross Margin, Excluding Depreciation & Amortization	40.7%	36.7%	38.8%	35.2%	28.7%	25.4%	21.1%	22.3%	24.6%
EBITDA Margin	35.0%	29.3%	30.0%	29.6%	24.0%	18.8%	18.1%	19.6%	21.9%
EBIT Margin	23.0%	9.9%	9.7%	10.1%	8.7%	4.3%	5.3%	7.5%	9.8%
Net Margin	19.2%	2.2%	3.5%	(3.9%)	1.4%	(10.6%)	2.1%	4.2%	6.3%
Finance Ratios									
Debt-Equity Ratio	1.3	1.5	1.4	1.4	1.3	1.4	1.3	1.2	1.1
Net Debt-Equity Ratio	1.1	1.1	1.1	1.2	1.1	1.2	1.1	1.0	0.8
Net Debt-to-Capital	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.4
Net Debt-to-EBITDA	2.9	4.8	5.8	5.5	5.2	6.7	6.6	5.2	4.0
Interest Coverage	12.2	2.4	1.3	1.1	1.1	0.8	1.3	1.8	2.3
Return Ratios									
ROIC	10.5%	3.2%	2.6%	3.0%	3.2%	1.7%	2.1%	3.3%	4.2%
ROE	20.4%	1.8%	2.3%	-2.8%	1.2%	-9.8%	2.0%	3.9%	5.8%
ROA	7.1%	0.6%	0.8%	-1.0%	0.4%	-3.2%	0.6%	1.3%	2.0%
FCF Yield	17.7%	7.2%	9.5%	5.5%	17.8%	7.5%	8.3%	12.9%	14.8%
Liquidity Ratios									
Current Ratio	0.9	1.2	1.0	1.2	1.2	1.2	1.0	1.6	1.6
Quick Ratio	0.9	1.1	1.0	1.1	1.1	1.1	1.0	1.5	1.5
Valuation									
EV/Sales	1.7	2.4	3.0	2.8	2.2	2.2	2.1	1.8	1.7
EV/EBITDA	5.0	8.3	9.9	9.6	9.3	11.7	11.6	9.4	7.6
EV/EBIT	7.6	24.4	30.9	28.0	25.5	51.4	39.8	24.5	17.0
P/E	4.4	53.1	41.9	N/M	81.6	N/M	55.2	26.3	16.9
P/CF	2.4	3.7	4.9	8.2	4.4	8.5	7.9	6.0	5.3
P/BV	0.9	0.9	1.0	1.0	1.0	1.1	1.1	1.0	1.0
Dividend Yield	5.2%	5.2%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
FCF Yield	17.7%	7.2%	9.5%	5.5%	17.8%	7.5%	8.3%	12.9%	14.8%

Source: Company data, QNB FS estimates

Detailed Financial Statements

Income Statement

In QR mn	2020	2021e	2022e	2023e	2024e
Revenue	2,998	3,042	3,263	3,340	3,396
COGS	2,666	2,783	2,927	2,916	2,924
Gross Profit	332	260	337	424	472
SG&A	213	198	204	210	215
Total Other Income	(305)	81	82	82	82
Net Finance Income (Expense)	(132)	(91)	(100)	(102)	(98)
Net Income*	(319)	64	135	210	254
EBITDA	564	549	641	730	781
EPS	(0.17)	0.03	0.07	0.11	0.14
DPS	0.00	0.00	0.00	0.00	0.00

Source: Company data, QNB FS estimates; Note: EPS based on current number of shares

Balance Sheet

In QR mn	2020	2021e	2022e	2023e	2024e
Current Assets					
Cash & Cash Equivalents	691	729	758	1,138	1,376
Financial Investments	365	395	460	525	590
Insurance & Accounts Receivables/Prepayments	1,427	1,736	1,824	1,868	1,900
Due From Related Parties	658	831	831	831	831
Inventories & Contract Assets	239	261	274	273	273
Total Current Assets	3,380	3,953	4,148	4,637	4,971
Non-Current Assets					
Financial Investments	369	401	401	401	401
Equity-Accounted Investees & JVs	15	18	24	30	36
Goodwill & Intangibles	304	304	304	304	304
Right of Use & Contract Assets	60	42	42	42	42
Property, Plant & Equipment	5,829	5,595	5,338	5,079	4,818
Non-Current Assets	6,577	6,359	6,108	5,855	5,601
Total Assets	9,956	10,313	10,256	10,491	10,571
Current Liabilities					
Short-Term Debt & Bank Overdraft	743	1,288	4	205	406
Insurance Payables, Accounts Payable & Accruals	2,017	2,418	2,513	2,542	2,573
Contract Liabilities & Lease Liabilities	37	35	35	35	35
Due to Related Parties	45	55	55	55	55
Current Liabilities	2,843	3,796	2,607	2,837	3,069
Non-Current Liabilities					
EOS/Provision for Decomm. Costs	133	140	140	140	140
Contract Liabilities	26	20	20	20	20
Long-Term Debt	3,702	3,058	4,055	3,850	3,444
Non-Current Liabilities	3,861	3,218	4,215	4,010	3,604
Total Liabilities	6,704	7,014	6,822	6,847	6,673
Shareholders' Equity					
Total Shareholders' Equity	3,252	3,298	3,434	3,644	3,898
Liabilities & Shareholders' Equity	9,956	10,313	10,256	10,491	10,571

Source: Company data, QNB FS estimates

Recommendations

Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price

OUTPERFORM	Greater than +20%
ACCUMULATE	Between +10% to +20%
MARKET PERFORM	Between -10% to +10%
REDUCE	Between -10% to -20%
UNDERPERFORM	Lower than -20%

Risk Ratings

Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals

R-1	Significantly lower than average
R-2	Lower than average
R-3	Medium / In-line with the average
R-4	Above average
R-5	Significantly above average

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