

GISS Alert – Generally In-line 1Q2023 Despite Earnings Miss; Maintain Accumulate

- **GISS posted a net profit of QR90.2mn in 1Q2023, down 19.5% YoY.** Reported earnings, however, came up short by 8.2% as compared to our forecast of QR98.2mn. *We also note that the previously reported 4Q2022 earnings of QR24.0mn is not strictly comparable given the IFRS 17-related restatement of the insurance segment.* GISS has not disclosed restated 4Q2022 numbers but we do note that the net effect of this restatement served to increase 1Q2022 earnings by QR28.8mn (previously reported 1Q2022 net income was QR83.3mn).
- **Overall top-line of QR836.6mn was in-line with our estimate of QR818.0mn (variation of 2.3%) with upside in insurance offsetting minor misses in aviation and drilling.** Group revenue grew 18.3% YoY from QR707.4mn in 1Q2022. We note that impact of the catering business has been removed from the top-line and other income statement items and is being treated as a discontinued item given Amwaj's pending merger (under IFRS 5 accounting treatment).
- **1Q2023 drilling revenue of QR337.4mn (5.2% YoY, 0.8% QoQ) was bang in-line with our estimate of QR338.5mn.** Rig utilization remained flattish at 96%, on a YoY basis, with the growth in revenue being helped by GDI's two lift boats that remained fully operational in 1Q2023 (vs. one of the liftboats becoming operational in mid-1Q2022). GDI's current fleet is fully operational after the deployment of GDI-8 in mid-4Q2022, except one onshore rig (GDI-4). Moreover, all five offshore rigs under the GulfDrill JV in the North Field project, are operating with 3Q2021 being the first full quarter of contribution.
- **Aviation revenue of QR226.2mn (9.6% YoY, -0.1% QoQ) was also in-line with our estimate of QR229.8mn (-1.6% variation).** Flying activity, both domestically and internationally (especially, Turkey that saw fleet expansion linked to better market penetration), saw substantial growth with actual flying hours up around 33% YoY in total (local up 23%, while international flying hours grew 50% YoY). The MRO business also remained strong despite a marginal yearly decline in its revenue.
- **1Q2023 insurance top-line of QR273.0mn (44.1% YoY) came in 9.4% above our estimate of QR249.6mn.** On a yearly basis, insurance segment saw significant growth from premiums from the medical insurance segment as Al Koot won new contracts during the quarter.
- **Catering, which is set to be merged, also saw decent growth with revenue of QR119.0mn (5.2% YoY).** This segment benefited from growth in the manpower business. *(continued on page 2)*

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- In terms of net income, relative to our model, drilling fell short, while other segments were generally in-line. We note that GISS did not disclose direct costs by segment so we could not determine gross margins by segment. *Please see page 3 for details on segmental revenue/costs/earnings.*
- Drilling reported a gross margin of 10.5% in 1Q2022 and it is possible that margins slipped YoY. Given that drilling finance costs of QR65.7mn (up significantly vs. QR29.3mn in 1Q2022, which also translated into a 11.5% QoQ increase) was almost in-line with our forecast of QR64.9mn (difference of 1.4%) and income from GulfDrill JV of QR10.0mn (vs. zero in 1Q2022 and only QR2.3mn in 4Q2022 due to mobilization costs/regular rig maintenance expenses) exceeded our estimate of QR7.3mn, some gross/operating margin erosion vs. our model is possible. Overall segment net loss came in at QR23.2mn (vs. losses of QR10.0mn in 1Q2022 and QR49.9mn in 4Q2022).
- The significant upside in insurance top-line did not really help its bottom-line vs. our forecast with segment earnings of QR33.4mn (down 29.5% YoY) falling short of our estimate of QR35.7mn (divergence of -6.4%). The company pointed to a significant decline in its investment income that fell roughly 71%YoY to ~QR12mn in 1Q2023 vs. QR40mn in 1Q2022.
- Aviation reported earnings of QR82.0mn (3.8% YoY, 71.8% QoQ) exceeded our estimate of QR79.0mn by 3.8%. We note 4Q2022 included a QR19.1mn net monetary loss from hyperinflation and a small impairment of QR2.2mn. 1Q2022 did not have any hyperinflation impact and in 1Q2023 this loss was only QR82,000.
- Catering earnings, which turned positive in 3Q2022 (QR1.8mn) and further rose in 4Q2022 (QR8.2mn) came in at QR4.7mn in 1Q2023. Catering earnings were only QR100,000 in 1Q2022.
- Net-net, we maintain our Accumulate rating and QR2.10 price target for now. We continue to envision an acceleration in momentum in the drilling segment – one onshore rig (GDI-4) is yet to be deployed and is expected to come on-line this year. Other segments should also contribute positively, while continued progress in costs reduction should help boost earnings. Interest expenses do remain a challenge given the company's significant debt load of QR4.3bn (most of which is related to drilling) and 1Q2023's quarterly finance charges' run-rate of QR67.5mn (up 127.8% YoY and 14.7% QoQ; ~75% of 1Q2023 net income). *Thus, favorable updates on debt restructuring, which was put on the back burner due to COVID-19, could please equity investors and we expect to hear something on this front this year. Moreover, completion of the merger of Amwaj (catering) with Shaqab/Atyab, could help drive sentiment. Finally, although GDI's offshore rigs are under 2-5 year contracts, current market rates are significantly higher. Thus, if the company is able to renegotiate these contract rates, that could be a major positive for the stock.*

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Income Statement (In QR Millions)

	1Q2022A	1Q2023A	1Q2023E	A Vs. E	YoY
Revenue	707.4	836.6	818.0	2.3%	18.3%
<i>Gulf Drilling International (GDI)</i>	320.8	337.4	338.5	-0.3%	5.2%
<i>Gulf Helicopters Company (GHC)</i>	206.4	226.2	229.8	-1.6%	9.6%
<i>Al Koot Insurance & Reinsurance (AKIR)</i>	189.5	273.0	249.6	9.4%	44.1%
COGS	571.3	674.1	618.3	9.0%	18.0%
Gross Profit	136.1	162.5	199.7	-18.6%	19.4%
Gross Margin	19.2%	19.4%	24.4%		
Net Income	112.1	90.2	98.2	-8.2%	-19.5%
Net Margin	15.9%	10.8%	12.0%		
<i>Gulf Drilling International (GDI)</i>	(10.0)	(23.2)	(14.3)	61.8%	133.0%
<i>Net Margin</i>	-3.1%	-6.9%	-4.2%		
<i>Gulf Helicopters Company (GHC)</i>	79.0	82.0	79.0	3.8%	3.8%
<i>Net Margin</i>	38.3%	36.3%	34.4%		
<i>Al Koot Insurance & Reinsurance (AKIR)</i>	47.5	33.4	35.7	-6.4%	-29.5%
<i>Net Margin</i>	25.1%	12.2%	14.3%		
<i>Corporate/Other</i>	(4.4)	(2.0)	(2.1)	-5.7%	-53.7%
EPS	0.06	0.05	0.05	-8.2%	-19.5%

Note: Addition of 1Q2022 segment revenue does not add up to consolidated revenue given catering inter-segment revenue

Recommendations	
<i>Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price</i>	
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	
<i>Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals</i>	
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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