

## Gulf International Services (GISS)

Recommendation	OUTPERFORM	Risk Rating	R-3
Share Price	QR36.65	Current Target Price	QR45.00
Implied Upside	22.8%	Old Target Price	QR53.00

### Lowering Estimates and TP; Upside Possible on Rig Deployments

*We are lowering our estimates & price target for GISS. While 2Q2016 was in-line with our model on an operating basis, net income fell short given interest expense and other income. We are lowering our estimates factoring in GDI's latest rig deployment schedule and recent segment-wise trends – we have cut our 2016-18e revenue and EBITDA estimates by 6% and 12%, respectively. We also reduce our price target to QR45. We note upside to our estimates is possible given previously idle assets (three offshore rigs/one accommodation jack-up) are now listed as warm stacked and thus could be potentially deployed in the medium term. We maintain our Outperform rating.*

#### Highlights

- **2Q2016 revenue/operating metrics in-line with our estimates:** However, net income fell short given interest expense/other income. *See page 2 for details.*
- **Lowering estimates factoring in recent results and rig deployment schedule; upside possible as previously idle assets (three offshore rigs/one accommodation jack-up) are now listed as warm stacked.** Given the lack of detailed quarterly segment-wise breakdown of KPIs, forecasting net income continues to remain a challenge. *We do note we have been accurate in terms of forecasting revenue, gross profits and EBITDA for 1Q2016 and 2Q2016 and net income for 1Q2016.* Our revised estimates factor in 2Q2016 results and GDI's rig deployment schedule. On the drilling front: (1) an older **onshore rig** remains off-contract, while GDI-8 began contributing from 2Q2016; (2) four **offshore rigs** previously idled in the shipyard, namely Al-Doha, Al-Rayyan, Les-Hat and Msheireb, have been listed as warm stacked as of the August fleet status report. While Msheireb is expected back in service in January 2017, the change in status of the other three rigs could augur deployment in the medium term and falls in line with our thesis that GISS potentially stands to gain 100%-market share of the offshore market. On the other hand, we note that Al-Wajba and Al-Zubarah were both undergoing underwater inspections in lieu of dry-docking in July, with the former moving back into contract in August but the latter now being repaired at the shipyard. Al-Jassra was contracted by Dolphin in late-February and Halul started contributing from April as anticipated; and (3) an **accommodation jack-up** (Zikreet) has been warm stacked, while the Rumailah **lift boat** remains out of commission for the rest of the year. The Al-Safliya lift boat, which was under construction, has also commenced activity as expected. While we will not adjust our estimates for potential redeployments until further evidence, we do consider the incremental warm stacking of the three offshore rigs and the accommodation jack-up a positive. *See page 2 for a detailed breakdown of segment forecasts for 2016.*

#### Catalysts

- **Stock price improvement hinged on sustained oil price recovery and a resumption of confidence in company performance.** GISS could also potentially gain 100%-offshore market share (2 rigs), allowing for redeployment of idling rigs.

#### Recommendation, Valuation and Risks

- **Recommendation and valuation:** *We rate GISS an Outperform with a QR45 price target.* GISS trades at 2017 & 2018 P/E multiples of 15.6x and 10.3x, respectively. While our price target offers upside, the stock remains in a "show me" mode.
- **Risks: Declining/volatile oil prices remain a substantial risk to regional equity prices.** Further decline in rig rates/rig utilizations could pressure the stock. GISS also faces concentration risk given its exposure to QP/affiliates.

#### Key Financial Data and Estimates

	2015	2016e	2017e	2018e
EPS (QR)	4.31	1.75	2.34	3.55
P/E (x)	8.5	21.0	15.6	10.3

Source: Company data, QNBFS 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)	72.00/28.65
3-m Avg. Volume (000)	336.9
Mkt. Cap. (\$ bn/QR bn)	1.9/6.8
FO Limit* (%)	25.0
Current FO* (%)	7.1
Shares Outstanding (mn)	185.8
1-Year Total Return (%)	(40.4)
Fiscal Year End	December 31

Source: Bloomberg (as of August 21, 2016), \*Qatar Exchange (as of August 21, 2016); Note: FO is foreign ownership

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## GISS Posts In-Line Operating Results for 2Q2016

GISS reported 2Q2016 net profit of QR81.8mn; operating metrics and revenue came in-line with our estimate. Net income inched up 3.6% QoQ (a decline of 67.2% YoY) in 2Q2016 vs. our estimate of QR108.0mn. The company's revenue increased by 6.7% QoQ (down 23.7% YoY) to QR827.5mn in 2Q2016, which was in-line with our estimate of QR868.1mn (variation of -4.7%). Gross profit and EBITDA were in-line with our estimates as well with divergences of -5.2% and -3.2%, respectively. The differential vs. our net income estimates came from primarily two sources – other income & net gain on financial assets (-QR9mn divergence) and net finance income (-QR12mn divergence). Our sense is that increase in GDI's leverage (primarily due to the addition of the Halul offshore rig) and its associated finance costs played a major part in this divergence.

### Estimates and Actuals

In QR '000 Except Otherwise Noted									2Q2016						
	2Q2015	2015	1Q2016	2Q2016	2Q2016e	3Q2016e	4Q2016e	2016	A Vs. E	QoQ	YoY	1H2016	1H2016e	A Vs. E	2H2016e
<b>Total Revenue</b>	1,084,555	4,164,250	775,168	827,466	868,125	794,461	867,750	3,264,845	-4.7%	6.7%	-23.7%	1,602,634	1,671,862	-4.1%	1,662,211
Insurance	168,386	685,621			163,334	130,010	158,901	548,497				259,586	325,104	-20.2%	288,911
Aviation	164,417	628,336			147,215	135,602	141,137	542,805				266,067	293,563	-9.4%	276,738
Catering	249,079	1,005,649			247,438	230,729	240,147	929,146				458,270	494,298	-7.3%	470,876
Drilling	502,673	1,844,644			310,137	298,120	327,566	1,244,397				618,711	558,898	10.7%	625,686
<b>COGS</b>	783,419	2,953,922	637,546	663,806	695,471	645,848	692,874	2,640,074	-4.6%	4.1%	-15.3%	1,301,352	1,366,906	-4.8%	1,338,722
Insurance	173,611	583,385			140,468	105,113	123,393	435,506				207,001	279,590	-26.0%	228,505
Aviation	100,771	401,435			97,162	89,269	91,073	354,995				174,653	193,751	-9.9%	180,342
Catering	226,569	886,159			220,220	193,251	199,535	776,766				383,980	439,925	-12.7%	392,786
Drilling	282,468	1,082,943			237,621	258,216	278,873	1,072,807				535,718	453,640	18.1%	537,089
<b>Gross Profit</b>	301,136	1,210,328	137,622	163,660	172,654	148,612	174,876	624,771	-5.2%	18.9%	-45.7%	301,282	304,956	-1.2%	323,489
<b>GM %</b>	27.8%	29.1%	17.8%	19.8%	19.9%	18.7%	20.2%	19.1%				18.8%	18.2%		19.5%
Insurance GM %	-3.1%	14.9%			20.3%	14.0%	19.2%	22.3%				20.3%	14.0%		20.9%
Aviation GM %	38.7%	36.1%	34.4%	34.4%	34.0%	34.2%	35.5%	34.6%				34.4%	34.0%		34.8%
Catering GM %	9.0%	11.9%	16.2%	16.2%	11.0%	16.2%	16.9%	16.4%				16.2%	11.0%		16.6%
Drilling GM %	43.8%	41.3%	13.4%	13.4%	23.4%	13.4%	14.9%	13.8%				13.4%	18.8%		14.2%
<b>Gross Profit Contribution</b>															
Insurance	-1.7%	8.4%	19.1%	16.1%	13.2%	16.8%	20.3%	18.1%				17.5%	14.9%		18.7%
Aviation	21.1%	18.7%	33.2%	27.9%	29.0%	31.2%	28.6%	30.1%				30.3%	32.7%		29.8%
Catering	7.5%	9.9%	27.0%	22.7%	15.8%	25.2%	23.2%	24.4%				24.7%	17.8%		24.1%
Drilling	73.1%	62.9%	30.2%	25.4%	42.0%	26.9%	27.8%	27.5%				27.5%	34.5%		27.4%
<b>SG&amp;A</b>	59,469	267,400	56,692	55,687	59,002	57,309	59,117	228,805	-5.6%	-1.8%	-6.4%	112,379	110,895	1.3%	116,426
SG&A %	5.5%	6.4%	7.3%	6.7%	6.8%	7.2%	6.8%	7.0%				7.0%	6.6%		7.0%
<b>Other Income &amp; Net Gain on Financial Assets</b>	23,165	(83,870)	12,963	1,639	10,501	7,301	7,301	29,204	-84.4%	-87.4%	-92.9%	14,602	21,355	-31.6%	14,602
<b>Net Finance Income (Expense)</b>	(15,143)	(57,630)	(14,963)	(27,831)	(16,106)	(28,932)	(28,927)	(100,653)	72.8%	86.0%	83.8%	(42,794)	(28,971)	47.7%	(57,859)
<b>Net Income</b>	249,689	801,428	78,930	81,781	108,047	69,672	94,134	324,516	-24.3%	3.6%	-67.2%	160,711	186,445	-13.8%	163,805
<b>NM %</b>	23.0%	19.2%	10.2%	9.9%	12.4%	8.8%	10.8%	9.9%				10.0%	11.2%		9.9%
<b>Insurance</b>	11,985	112,374	28,057	29,070	25,220	27,165	37,775	122,067				57,127	50,198	13.8%	64,940
Insurance NM %	7.1%	16.4%	21.6%	22.4%	15.4%	20.9%	23.8%	22.3%				22.0%	15.4%		20.9%
<b>Aviation</b>	57,270	193,210	37,689	39,051	45,888	38,533	42,264	157,536				76,740	91,506	-16.1%	80,796
Aviation NM %	34.8%	30.7%	28.3%	29.4%	31.2%	28.4%	29.9%	29.0%				28.8%	31.2%		31.2%
<b>Catering</b>	33,277	115,584	34,252	35,490	26,476	34,985	38,118	142,845				69,742	52,891	31.9%	73,103
Catering NM %	13.4%	11.5%	14.9%	15.5%	10.7%	15.2%	15.9%	15.4%				15.2%	10.7%		15.4%
<b>Drilling</b>	159,460	431,167	(7,269)	(7,531)	23,240	(16,962)	(9,975)	(41,736)				(14,800)	16,458	-189.9%	(26,936)
Drilling NM %	31.7%	23.4%	-2.3%	-2.4%	7.5%	-5.7%	-3.0%	-3.4%				-2.4%	2.9%		2.9%
Unallocated (Plug)	(12,303)	(50,907)	(781)	(27,317)	(12,778)	(14,049)	(14,049)	(56,196)				(28,098)	(6,815)		(28,098)
<b>EPS (QR)</b>	1.34	4.31	0.42	0.44	0.58	0.37	0.51	1.75	-24.3%	3.6%	-67.2%	0.86			0.88
<b>EBITDA</b>	391,936	1,380,390	224,073	263,761	272,573	248,406	272,868	1,009,108	-3.2%	17.7%	-32.7%	487,834			521,274
EBITDA Margin %	36.1%	33.1%	28.9%	31.9%	31.4%	31.3%	31.4%	30.9%				30.4%			31.4%

Source: Company data, QNBFS estimates

## Detailed Financial Statements

### Income Statement

In QR mn	FY2014	FY2015	FY2016e	FY2017e	FY2018e
<b>Revenue</b>	<b>3,906</b>	<b>4,164</b>	<b>3,265</b>	<b>3,450</b>	<b>4,096</b>
Gulf Drilling International (GDI)*	1,473	1,845	1,244	1,347	1,907
Gulf Helicopters Company (GHC)	644	628	543	581	621
Amwaj Catering Company (ACS)	1,056	1,006	929	957	986
Al Koot Insurance & Reinsurance (AKIR)	733	686	548	565	582
<b>COGS</b>	<b>2,710</b>	<b>2,954</b>	<b>2,640</b>	<b>2,692</b>	<b>3,090</b>
<b>Gross Profit</b>	<b>1,196</b>	<b>1,210</b>	<b>625</b>	<b>758</b>	<b>1,006</b>
SG&A	217	267	229	234	252
Total Other Income	89	(84)	29	29	29
Net Finance Income (Expense)	(27)	(58)	(101)	(118)	(123)
One-Offs/Non-Recurring Items	269	0	0	0	0
Income from JVs	100	0	0	0	0
<b>Net Income</b>	<b>1,410</b>	<b>801</b>	<b>325</b>	<b>435</b>	<b>661</b>
<b>Net Income (Clean)</b>	<b>1,140</b>	<b>801</b>	<b>325</b>	<b>435</b>	<b>661</b>
<b>EBITDA</b>	<b>1,818</b>	<b>1,380</b>	<b>1,009</b>	<b>1,161</b>	<b>1,405</b>
<b>EBITDA (Clean)</b>	<b>1,549</b>	<b>1,380</b>	<b>1,009</b>	<b>1,161</b>	<b>1,405</b>
<b>DPS (QR)</b>	<b>5.50</b>	<b>1.00</b>	<b>1.00</b>	<b>1.25</b>	<b>1.50</b>

Source: Company data, QNBFS estimates; Note: EPS based on current number of shares, \*GDI results consolidated from May 1, 2014

### Balance Sheet

In QR mn	FY2014	FY2015	FY2016e	FY2017e	FY2018e
<b>Current Assets</b>					
Cash & Cash Equivalents	1,087	961	1,505	2,184	2,998
Investments Held for Trading	218	206	207	207	207
Insurance Contract Receivables & A/R	946	1,170	1,137	1,197	1,378
Due From Related Parties	634	598	490	490	490
Inventories	203	222	224	229	262
<b>Total Current Assets</b>	<b>3,089</b>	<b>3,158</b>	<b>3,563</b>	<b>4,306</b>	<b>5,336</b>
<b>Non-Current Assets</b>					
Available for Sale Investments	300	314	308	308	308
Held to Maturity Investments	85	86	86	86	86
Investment in Joint Ventures	-	-	-	-	-
Investment Properties	1	-	-	-	-
Goodwill	313	307	305	304	304
Property, Plant & Equipment	7,037	7,364	7,593	7,364	7,195
<b>Non-Current Assets</b>	<b>7,738</b>	<b>8,071</b>	<b>8,292</b>	<b>8,062</b>	<b>7,892</b>
<b>Total Assets</b>	<b>10,826</b>	<b>11,229</b>	<b>11,854</b>	<b>12,368</b>	<b>13,228</b>
<b>Current Liabilities</b>					
Short-Term Debt	909	1,467	798	798	798
Insurance Payables & Accounts Payable	1,719	2,050	1,860	1,910	2,090
Due to Related Parties	11	20	9	9	9
<b>Current Liabilities</b>	<b>2,638</b>	<b>3,536</b>	<b>2,667</b>	<b>2,717</b>	<b>2,897</b>
<b>Non-Current Liabilities</b>					
Employees End of Service Benefits	64	75	71	71	71
Long-Term Debt	3,946	3,690	5,057	5,271	5,523
Non-Current Liabilities	4,010	3,765	5,128	5,342	5,594
<b>Total Liabilities</b>	<b>6,649</b>	<b>7,301</b>	<b>7,795</b>	<b>8,060</b>	<b>8,491</b>
<b>Shareholders' Equity</b>					
<b>Total Shareholders' Equity</b>	<b>4,178</b>	<b>3,928</b>	<b>4,059</b>	<b>4,309</b>	<b>4,737</b>
<b>Liabilities &amp; Shareholders' Equity</b>	<b>10,826</b>	<b>11,229</b>	<b>11,854</b>	<b>12,368</b>	<b>13,228</b>

Source: Company data, QNBFS 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

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

### Risk Ratings

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

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

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