IGRD Alert – 1Q2023 Miss As Post World-Cup Activity Slows; Moving to Accumulate from Outperform

- **Estithmar's 1Q2023 results fell shy of our model both at the top- and the bottom-line. While margins came in better-than-expected, the top-line miss led to lower-than-expected earnings.** Earnings increased 10.2%/166.4% YoY/QoQ to QR101.2mn, it was below our estimate of QRQR125.7mn; net income was helped by uncharacteristically strong margins in the contracting & services segment. **Revenue was off the mark, declining 9.5%/36.2% YoY/QoQ to QR766.8bn vs. our estimate of Q1.26bn.**
- **With overall revenue lower, group net margin was surprisingly stronger at 13.4% vs. 9.6% expected driven by the contracting & industries division** which registered a markedly higher net margin of 30.6% vs 3.9% expected. While a positive development, this is somewhat of a surprise given that construction is generally a low-margin business with upper single-digit margins usually considered industry-leading. Specifically, IGRD's construction & industries division's net margin was -2.5% in 1Q2022 and 2.8% in 4Q2022, and it averaged 4.0% between FY2019-22. Thus, the bump up in 1Q2023 margin could be unsustainable and we will try to get more color from management.
- **Barring the healthcare division, where The View hospital had its first full quarter of operations, albeit at significantly reduced capacity, all other segments recorded significantly lower revenue than we had anticipated.** The healthcare division recorded revenue of QR17.1mn, while the equally new ventures/tourism division registered sales of QR72.6mn. Both divisions recorded loses of QR45.3mn and QR10.7mn, respectively. We note that for the tourism division, the loss was incurred despite QR40mn of government support. The View hospital was hardly operational as it was still going through final fit-out touches for the better part of 1Q2023. So, there remains significant scope for operations to ramp up. **With another hospital, KMC, expected to start operations later this year, management expects the healthcare division to generate over QR900mn in revenue when operations stabilize in the medium-term**. While we are a bit more concerned with the tourism division, the prospect of growing tourists arrivals is likely to improve the division's performance dynamics. **Management expects annual revenue of around QR340mn from the ventures/tourism segment when operations stabilize.**
- **Traditional businesses' revenue exhibited a marked decline from last year's World Cup-induced boom.** The contracting & industries segment registered a 16.7%/41.8% YoY/QoQ revenue decline to QR362.7mn in 1Q2023, but turned a loss of QR11.1mn in 1Q2022 to a profit of QR111.2mn in 1Q2023 – the margin blew out expectations and we think it is not sustainable. Meanwhile, the services segment revenue fell 7.4%/46.4% YoY/QoQ to QR397.7mn and profit declined 17.4%/31.8% YoY/QoQ to QR56.7mn.
- **Group debt levels and capital needs are growing – leverage metrics have gradually weakened since last year but they remain reasonable.** Coupled with rising rates, finance costs spiked almost threefold YoY to Q27.3mn in 1Q2023, a 20.0% QoQ increase. Net debt now stands at QR1.8bn compared with QR1.7bn at end-FY2022 and QR934.4mn at the beginning of FY2022. IGRD's net debt/equity ratio at end-1Q2023 was 39.3% from 38.7% at end-FY2022 and 27.7% at end-1H2022. With the recent announcement of new offshore projects (Saudi Arabia and Maldives) we expect more capital raises in the future, with the initial effect of equity and/or earnings dilution. Coupled with no or limited distributions to shareholders, IGRD's share price may face near-term headwinds. We remain bullish on its above-average growth in the medium-term, however. *(continued on Page 2)*

QNB FINANCIAL SERVICES

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- **We are changing our rating from Outperform to Accumulate – IGRD's current price implies upside of 16.3% to our existing price target QR2.361.** Our thesis is that in the medium-term, higher-margin divisions – healthcare, tourism and services – should offset some of the weakness that we see in its traditional business of contracting & industries. *We note that we expect to adjust our TP as well in a subsequent note primarily to account for capital markets developments related to the latest cost of capital and market multiples signals.* We note that growth companies or higher-duration assets such as IGRD have been adversely affected by the faster-than-expected ratcheting up of global interest rates. **Overall, we like IGRD as its future growth is geared towards higher-margin sectors.**

IGRD 1Q2023 Segment Performance

	1Q2022	4Q2022	1Q2023	YoY	QoQ
Revenue	**847.20**	**1,202.26**	**766.77**	-9.5%	-36.2%
Services	429.66	742.59	397.72	-7.4%	-46.4%
Contracting & Industries	435.57	622.88	362.75	-16.7%	-41.8%
Healthcare	8.73	10.22	17.13	96.3%	67.6%
Ventures/Tourism	-	103.88	72.60	N/M	-30.1%
Corporate/Eliminations	(26.76)	(277.31)	(83.43)	N/M	N/M
Net Profit	**93.02**	**35.14**	**102.46**	10.2%	191.6%
Services	68.66	83.20	56.74	-17.4%	-31.8%
Contracting & Industries	(11.08)	17.24	111.17	N/M	544.7%
Healthcare	0.81	0.31	(45.27)	N/M	N/M
Ventures/Tourism	39.66	(23.76)	(10.74)	N/M	N/M
Corporate/Eliminations	(5.03)	(41.85)	(9.43)	N/M	N/M
Minorities	**1.17**	**(2.85)**	**1.25**	6.7%	N/M
Earnings to Equity holders	**91.85**	**37.99**	**101.21**	**10.2%**	**166.4%**

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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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