

GFH Financial Group

Strong growth in profitability despite volatile market conditions

1Q23 Net Profit higher than our estimates

GFH Financial Group's (GFH/the Company) net profit reported strong growth of 25.6% YOY to USD 24 Mn in 1Q23, higher than our estimate of USD 19 Mn. The Company's net profit is mainly driven by robust growth in overall income partially offset by an increase in finance costs and operating expenses.

P&L highlights

GFH's total income rose 31.7% YOY to USD 87 Mn in 1Q23 mainly due to the robust growth in income from investment banking, commercial banking, real estate, and proprietary & co-investments income partially offset by a decline in treasury and other income segment. The company's income from proprietary and co-investments almost doubled to USD 14 Mn in 1Q23 from USD 7 Mn in 1Q22. Similarly, income from investment banking segment rose 82.7% YOY to USD 45 Mn in 1Q23 mainly due to increase in investment banking activity in the region resulting in growth in deal related income and fee income. Real estate income rose 47.1% YOY to USD 5 Mn in 1Q23 whereas commercial banking income increased 29.0% YOY to USD 25 Mn attributable to healthy growth in income from financing and investments and fee income. However, treasury and other income reported a loss of USD 2 Mn in 1Q23 compared to a gain of USD 12 Mn in 1Q22 due to a significant rise in finance expense. The company's operating expenses rose 19.8% YOY to USD 41 Mn in 1Q23 with a cost-to-income ratio of 47.3% in 1Q23 as compared to 52.0% in 1Q22. As a result, operating profit rose 44.5% YOY to USD 46 Mn in 1Q23 with an 467 bps YOY change in operating profit margin to 52.7% in 1Q23. Furthermore, the Company's finance cost rose significantly to USD 21 Mn in 1Q23 compared to USD 12 Mn in 1Q22 due to the higher interest rates in the economy. Moreover, impairment allowance declined to USD 0.6 Mn in 1Q23 as compared to USD 1.4 Mn in 1Q22. Thus, total expenses rose from USD 12 Mn in 1Q22 to USD 21 Mn in 1Q23.

Balance Sheet highlights

GFH's assets under management stood at USD 7.9 Bn in 1Q23 as compared to USD 7.8 Bn in 1Q22 whereas the group charged management fees and performance fees of USD 2.9 Mn in 1Q23 as against USD 23 Mn in 4Q22. In addition, the group's CET 1 ratio and capital adequacy ratio stood healthy at 13.6% and 14.4% respectively in 1Q23. The group's interest-earning assets rose 3.6% QOQ to USD 7.9 Bn in 1Q23. GFH's total equity declined 1.3% QOQ to USD 1.1 Bn in 1Q23 due to the approval of dividends.

Target price and recommendation

We maintain our BUY rating on GFH with a target price of AED 1.30. The Company reported a robust performance across its segments despite volatility in the global market. GFH is focused on strategic investments by aiming to invest in the defensive sector and diversify its investment. This will improve the company's performance in an unstable economic environment. The group managed USD 17.6 Bn of assets and funds, including a global portfolio of investments in healthcare, logistics, education, and technology across Europe, North America, and the MENA region. The Company's total assets rose 6.1% YOY to USD 10.4 Bn in 1Q23 while the

Rating : BUY

First Look Note – 1Q23

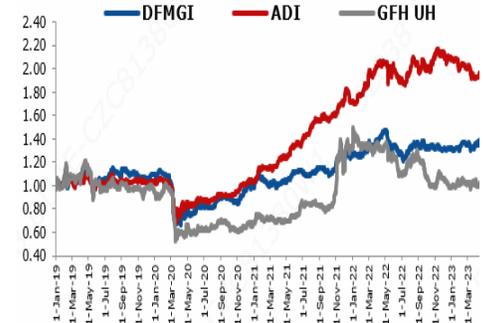
Sector: Financial Services

Recommendation

Current Price (23-May-23)	0.938
Target Price (AED)	1.30
Upside/Downside (%)	+39%

Stock Information

Market Cap (mm)	3,748.19
Paid Up Capital (mm)	1,015.61
52 Week High	1.18
52 Week Low	0.87
3M Avg. daily value (AED)	3,185,984



Financial Ratios

Dividend Yield (12m)	5.97
Dividend Pay-out (%)	61.51
Price-Earnings Ratio (x)	8.99
Price-to-Book Ratio (x)	1.01
Book Value (AED)	0.26
Return-on Equity (%)	9.43
Earning Per Share (AED)	0.03
Beta	1.32

Stock Performance

5 Days	4.82%
1 Months	5.16%
3 Months	6.07%
6 Months	0.51%
1 Year	-10.28%
Month to Date (MTD)	6.77%
Quarter to Date (QTD)	3.93%
Year to Date (YTD)	10.01%

AUM increased 38.1% YOY to USD 7.9 Bn in 1Q23. However, the company's asset yield on financing income declined 11 bps on a QOQ basis and stood at 4.76% whereas the cost of funds also declined by 76 bps on QOQ basis to 0.63% in 1Q23. On the other hand, GFH's asset quality moderated with an NPL ratio of 6.2% in 1Q23 compared to 4.6% in 4Q22 whereas the provision coverage ratio declined from 92.5% in 4Q22 to 66.6% in 1Q23. In addition, stage 2 loans as a percentage of total loans increased from 9.6% in 4Q22 to 11.3% in 1Q23. However, the company maintained healthy capitalization with a capital adequacy ratio of 14.39% and a liquidity coverage ratio of 179%. Strong Investment Banking activity in the region boosted the Company's deal-related income in 1Q23. Favourable regional dynamics in the Middle East region resulted in 632 M&A deals in 2022 driven by investments from Private Equity and Sovereign Wealth Funds further supported by elevated energy prices and improvement in liquidity on the back of fiscal reform. In addition, the MENA region saw a record 51 IPOs in 2022 with a proceed of USD 22.0 Bn. Furthermore, we expect the investment banking activity growth to remain robust in 2023. Thus, based on our analysis, we maintain our BUY rating on the stock.

GFH - Relative Valuation

(at CPM)	2018	2019	2020	2021	2022	2023F
PE	7.95	13.07	19.26	9.85	9.67	9.44
PB	0.93	0.98	1.07	1.02	0.98	0.90
Dividend Yield	3.5%	3.5%	1.9%	4.7%	6.2%	6.2%

FABS estimate & Co Data
GFH - P&L

USD Mn	1Q22	4Q22	1Q23	1Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Investment Banking Income	25	47	45	23	99.3%	82.7%	-3.6%	121	130	8.0%
Commercial banking income	20	21	25	31	-18.9%	29.0%	24.2%	79	86	9.5%
Inc. from proprietary & co-invest.	7	57	14	12	17.3%	96.3%	-76.3%	104	95	-9.2%
Real Estate Income	3	-5	5	2	107.6%	47.1%	NM	21	22	4.4%
Treasury and other income	12	31	-2	36	NM	NM	NM	117	89	-23.5%
Total income	66	151	87	104	-16.6%	31.7%	-42.3%	442	423	-4.3%
Operating expenses	34	64	41	35	16.0%	19.8%	-35.8%	148	156	5.7%
Operating Profit	32	87	46	69	-33.4%	44.5%	-47.1%	294	266	-9.3%
finance expenses	11	79	21	47	-55.4%	88.9%	-73.8%	193	151	-21.6%
impairment allowance	1	3	1	4	-82.7%	-54.1%	-79.0%	3	15	NM
Total Expense	12	82	21	50	-57.4%	72.9%	-74.0%	196	166	-15.4%
Profit for the period	19	4	24	19	31.8%	26.3%	NM	98	100	2.8%
Non-Controlling Interest	0	2	0	0	NM	86.6%	-80.5%	7	7	0.0%
Profit to shareholders	19	2	24	19	29.5%	25.6%	NM	90	93	3.0%

FABS Estimates & Co Data
GFH - Margins

	1Q22	4Q22	1Q23	YOY Ch	QOQ Ch	2022	2023F	Change
OPM	48.0%	57.5%	52.7%	467	-480	66.5%	63.0%	-350
Net Margin	29.0%	1.3%	27.6%	-134	2,627	20.4%	22.0%	157

FABS estimate & Co Data

Valuation:

We use Residual Income and Relative Valuation (RV) method to value GFH. We have assigned 70% weight to Residual Income and 30% to RV method.

Valuation Method	Target	Weight	Weighted Value
Residual Income	1.21	70.0%	0.85
Relative Valuation	1.50	30.0%	0.45
Weighted Average Valuation (AED)			1.30
Current market price (AED)			0.94
Upside/Downside (%)			38.6%

1) Residual Income Method:

We have discounted the economic profit/excess equity using the cost of equity of 10.3%. Cost of equity is calculated by using 10-year government bond yield of 5.9%, beta of 0.7 and equity risk premium of 6.0%. We have assumed Bahrain 10Y Government Bond yield for valuing the company. Also, assumed a terminal growth rate of 1.5%.

Sum of PV (USD, Mn)	-43
Terminal value (USD, Mn)	-20
Required Capital	940
FV to Common shareholders (USD, Mn)	976
No. of share (Mn)	3,833
Current Market Price (AED)	0.94
Fair Value per share (AED)	1.21

Residual Income method

(All Figures in USD Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
Net profit	93	106	114	133	142
Excess return excess capital	-14	-19	-24	-31	-38
Adjusted net profit	79	87	90	102	114
Equity charge	-97	-100	-103	-106	-109
Economic Profit	-18	-13	-13	-4	-4
Discounting Factor	0.94	0.85	0.77	0.70	0.63
Present value of excess equity	-17	-11	-10	-3	-3

2) Relative Valuation:

We have used local as well as international peers to value GFH's different segments. It owns a stake in Khaleeji Commercial Bank and it is valued using regional peers with a PB multiple of 1.0x. Investment Banking Segment is valued using the PE multiple of regional and global peers with a median PE multiple of 9.4x. Treasury and Hold Co. Segment is valued using international peers using a median PB multiple of 0.9x.

Commercial bank	Market (USD Mn)	PB (x)		PE (x)	
		2023	2024	2023	2024
Bank Muscat	5,614	1.1	1.0	11.7	9.6
RAK Bank	2,223	0.9	0.8	7.0	7.7
Mashreq Bank	6,281	1.0	0.9	7.0	7.5
Commercial Bank of Dubai	3,657	1.1	1.0	3.3	3.2
Bank Aljazira	3,927	1.1	1.0	13.4	11.0
Qatar Islamic Bank	15,701	0.9	0.9	8.1	8.8
Average		1.0x	1.0x	8.4x	8.0x
Median		1.0x	1.0x	7.5x	8.3x
Max		1.1x	1.0x	10.8x	9.4x
Min		1.0x	0.9x	7.0x	7.5x

Investment Bank	Market (USD Mn)	PB (x)		PE (x)	
		2023	2024	2023	2024
Jefferies Financial Group	7,514	0.8	0.7	10.8	7.4
Stifel Financial Group	6,230	1.2	1.1	9.1	8.2
Guotai Junan Securities	16,613	0.8	0.7	7.4	7.0
Lazard	2,916	4.8	3.9	12.5	10.0
EFG Hermes holdings	703	1.2	1.1	9.7	8.3
Lincoln National Corporation	4,342	1.2	1.0	3.3	2.9
Average		1.7x	1.4x	8.8x	7.3x
Median		1.2x	1.0x	9.4x	7.8x
Max		1.2x	1.1x	10.5x	8.3x
Min		0.9x	0.8x	7.8x	7.1x

Treasury and Holdco	Market (USD Mn)	PB (x)		PE (x)	
		2023	2024	2023	2024
Nomura Holdings	12,183	0.6	0.5	12.6	9.5
Canaccord Genuity Group	696	1.0	1.0	-	8.1
Barclays PLC	30,122	0.4	0.4	5.2	4.6
Assetmark Financial holding	2,168	1.7	1.5	15.0	13.9
PNC financial services	54,820	1.3	1.2	9.3	9.0
Insignia Financial	1,319	0.9	0.9	32.6	24.7
Average		1.0x	0.9x	14.9x	11.6x
Median		0.9x	0.9x	12.6x	9.2x
Max		1.2x	1.1x	15.0x	12.8x
Min		0.6x	0.6x	9.3x	8.3x

FAB Securities Awards



Best Brokerage House in UAE 2016 & 2017 by "Banker Middle East"



Best Brokerage House in UAE 2016, 2017, 2019 and 2020 by "IFA"



Best Brokerage in the UAE 2016 By "Global Investor/ ISF ME Awards"



Best Research House in UAE 2016 and 2020 by "IFA"



Best New Mobile Application in UAE 2016 by "IFA"



Best Equity Finance Company in UAE 2016 by "IFA"