

GFH Financial Group

Robust growth in Investment Banking income drove profitability

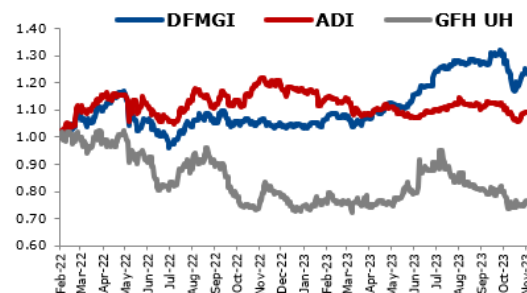
Current Price
AED 0.91

Target Price
AED 1.30

Upside/Downside (%)
+43%

Rating
BUY

- GFH reported more than double growth in Investment Banking revenue due to solid growth in deal-related income driven by closing transactions of US opportunistic Fund, Student Housing Fund, Saudi Food Logistics Fund in 3Q23.
- GFH maintained healthy capitalization with a CET 1 ratio of 14.7% and capital adequacy ratio of 15.6% in 3Q23.
- GFH's total assets rose 2.0% QOQ and 17.1% YOY to USD 10.5 Bn in 3Q23 whereas AUM's increased 9.8% QOQ and 25.9% YOY to USD 9.3 Bn in 3Q23.
- According to GFH's strategy to invest in diversified sectors and expansion across different geographies, GFH made two strategic acquisitions in the KSA's logistics sector during 3Q23.



3Q23 Net Profit lower than our estimate

GFH Financial Group's (GFH/the Company) net profit rose marginally 1.2% YOY to USD 24 Mn in 3Q23, lower than our estimate of USD 27 Mn. The Company's net profit is mainly driven by the strong income from the Investment Banking segment and lower losses in the Treasury segment in 3Q23 partially offset by a decline in income from Commercial Banking, Real Estate, and income from Proprietary and Co-investment business along with increase in operating expenses, finance cost, and impairments.

P&L Highlights

GFH's total income rose 32.8% YOY to USD 88 Mn in 3Q23 due to robust growth in Investment Banking income and a decline in losses from the Treasury segment partially offset by a decline in Commercial Banking, Real Estate, and Proprietary and Co-investment business income. Investment Banking income grew significantly from USD 29 Mn in 3Q22 to USD 76 Mn in 3Q23 due to strong growth in deal-related income. Commercial Banking income declined from USD 22 Mn in 3Q22 to USD 7 Mn in 3Q23 due to higher finance expenses owing to the high cost of funds driven by a rise in benchmark rates. Meanwhile, income from Proprietary and Co-investments declined 16.2% YOY to USD 10 Mn in 3Q23 driven by a decline in investment income. Moreover, Real Estate income fell to USD 5 Mn in 3Q23 compared to USD 17 Mn in 3Q22. On the other hand, loss from Treasury business narrowed to USD 10 Mn in 3Q23 from USD 13 Mn in 3Q22 due to higher finance income partially offset by an increase in finance expenses. Furthermore, the Company's operating expenses rose from USD 24 Mn in 3Q22 to USD 42 Mn in 3Q23 with a cost-to-income ratio of 47.8% in 3Q23 compared to 37.0% in 3Q22. Operating profit rose 10.2% YOY to USD 46 Mn in 3Q23. In addition, the Company's finance cost increased 24.0% YOY to USD 15 Mn in 3Q23 due to higher benchmark rates. Whereas, impairments more than doubled to

Stock Information	
Market Cap (AED, mm)	3,491.49
Shares Outstanding(mm)	3,832.59
52 Week High	1.20
52 Week Low	0.85
3M Avg. daily value (AED)	3,175,139

3Q23 Result Review (USD, Mn)	
Total Assets	10,542
Total Liabilities	9,464
Total Equity	1,078
Total Income	88
Net Profit	24

Financial Ratios	
Dividend Yield (12m)	6.41
Dividend Pay-out (%)	61.51
Price-Earnings Ratio(x)	8.26
Price-to-Book Ratio (x)	0.96
Book Value (AED)	0.26
Return-on Equity (%)	10.56

Stock Performance	
5 Days	-0.87%
1 Months	0.66%
3 Months	-6.66%
6 Months	-4.91%
1 Year	-5.10%
Month to Date (MTD%)	-0.22%
Quarter to Date (QTD%)	-6.56%
Year to Date (YTD%)	2.47%

USD 7 Mn in 3Q23 from USD 3 Mn in 3Q22. The Company's finance cost and impairment allowances were also affected due to costs from newly acquired subsidiaries. Share of profit attributable to non-controlling interest holders stood USD 2 Mn in 3Q22 compared to a loss of USD 0.4 Mn in 3Q23.

Balance Sheet Highlights

GFH's assets under management stood at USD 9.3 Bn in 3Q23 compared to USD 8.4 Bn in 2Q23 whereas the group charged management and performance fees of USD 5.1 Mn in 3Q23 as against USD 6.7 Mn in 2Q23. In addition, the group's CET 1 ratio and capital adequacy ratio stood healthy at 14.7% and 15.6% respectively in 3Q23. The group's interest-earning assets rose 0.6% QOQ to USD 8.2 Bn in 3Q23. GFH's total equity rose 2.5% QOQ and 5.6% YOY to USD 1.1 Bn in 3Q23.

Target Price and Rating

We maintain our BUY rating on GFH with a target price of AED 1.30. GFH reported a stable financial performance in 3Q23 driven by solid contribution from the Investment Banking segment partially offset by a decline in income from other segments owing to the high cost of funds. Income from the Investment Banking segment more than doubled in 3Q23 compared to 3Q22 owing to a solid rise in asset management fees and placement of deals. Investment Banking income contributed 78.8% to the total income in 3Q23. The Company closed three new transactions such as the US Opportunistic Fund, Student Housing Fund, and Saudi Food Logistics Fund driving the deal-related income in 3Q23. A positive economic outlook in the region will further boost the GFH's Investment Banking revenue. The group managed USD 19 Bn of assets and AUMs in the MENA region. The Company's total assets rose 2.0% QOQ and 17.1% YOY to USD 10.5 Bn in 3Q23 whereas AUM's increased 9.8% QOQ and 25.9% YOY to USD 9.3 Bn in 3Q23. Moreover, the Company's asset yield on financing income rose 68 bps QOQ to 5.73% in 3Q23 whereas cost of funds grew 17 bps QOQ to 0.75% in 3Q23. In addition, GFH's asset quality declined as NPLs rose to 8.5% in 3Q23 as compared to 5.9% in 2Q23 whereas provision coverage fell to 48.6% in 3Q23 from 74.5% in 2Q23. Whereas stage 2 loans as a percentage of gross loans rose to 19.4% in 3Q23 compared to 18.1% in 2Q23. However, the Company maintained a healthy capitalization with a CET 1 ratio of 14.7% and a capital adequacy ratio of 15.6% in 3Q23. According to the Company's strategy of investment in diversified sectors and expansion across different geographies, GFH made two strategic acquisitions in 3Q23. GFH's subsidiary 'GFH Partners' acquired a USD 150 Mn logistics portfolio which comprises of mission-critical assets. The stable income-yielding assets of the acquired company are spread across Saudi Arabia and the UAE in the key cities. In addition, GFH also signed an agreement to acquire a food services and logistics business 'the Company' in the KSA. GFH will benefit from investment in Saudi's logistics sector owing to the solid outlook of the KSA's non-oil sector growth. Thus, based on our analysis, we assign a BUY rating on the stock.

GFH - Relative valuation

(at CMP)	2018	2019	2020	2021	2022	2023F
PE	7.70	12.65	18.64	9.54	9.36	8.11
PB	0.90	0.95	1.04	0.99	0.95	0.88
Cash dividend yield	3.4%	3.4%	1.9%	4.8%	6.4%	6.4%

FABS Estimates & Co Data

GFH – P&L

USD mm	3Q22	2Q23	3Q23	3Q23F	Var.	YOY Ch	QOQ Ch	2022	2023F	Change
Investment Banking Income	29	45	76	44	71.9%	164.6%	66.7%	121	224	85.9%
Commercial banking income	22	16	7	12	-42.2%	-68.4%	-56.8%	79	58	-26.7%
Income from proprietary and co-investments	11	14	10	16	-42.0%	-16.2%	-33.5%	104	51	-50.6%
Real Estate Income	17	10	5	8	-37.6%	-70.0%	-48.5%	21	29	38.1%
Treasury and other income	-13	1	-10	9	NM	-24.9%	NM	117	-8	NM
Total income	66	87	88	89	-2.0%	32.8%	0.8%	442	355	-19.6%
Operating expenses	24	37	42	40	4.0%	71.3%	12.5%	148	163	10.3%
Operating Profit	41	50	46	49	-6.9%	10.2%	-7.9%	294	192	-34.8%
Finance expenses	12	11	15	16	-3.7%	24.0%	43.6%	193	62	-67.8%
Impairment allowance	3	6	7	4	71.5%	NM	5.4%	3	20	NM
Total Expense excl. OPEX	15	17	22	20	11.1%	41.8%	29.3%	196	83	-57.9%
Profit for the period	26	33	24	29	-18.9%	-8.5%	-27.1%	98	109	11.7%
Non-Controlling Interest	2	2	0	2	NM	NM	NM	7	4	-41.5%
Profit to shareholders	24	31	24	27	-11.3%	1.2%	-20.6%	90	105	16.0%

FABS estimate & Co Data

GFH - Margins

	3Q22	2Q23	3Q23	YOY Ch	QOQ Ch	2022	2023F	Change
Operating margin	63.0%	57.2%	52.2%	-1,072	-495	66.5%	54.0%	-1,250
Net profit margin	36.5%	35.3%	27.8%	-869	-748	20.4%	29.5%	908

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	1.15	70.0%	0.81
Relative valuation	1.63	30.0%	0.49
Weighted Average Valuation (AED)			1.30
Current market price (AED)			0.91
Upside/Downside (%)			+43%

1) Residual Income Method:

We have discounted the economic profit/excess equity using the cost of equity of 10.8%. The cost of equity is calculated by using a 10-year government bond yield of 7.1%, beta of 0.75 and equity risk premium of 5.0%. We have assumed Bahrain's 10Y Government Bond yield for valuing the company. Also, assumed a terminal growth rate of 2.0%.

Sum of PV (USD, Mn)	-77
Terminal value (USD, Mn)	-197
Required Capital	1,050
FV to Common shareholders (USD, Mn)	1,204
No. of share (Mn)	3,833
Current Market Price (AED)	0.91
Fair Value per share (AED)	1.15

Residual Income Method

(All Figures in USD Mn)	FY 2023E	FY 2024E	FY 2025E	FY 2026E	FY 2027E
Net profit	105	109	121	152	135
Excess return excess capital	-8	-9	-9	-14	-16
Adjusted net Profit	97	101	112	138	119
Equity Charge	-114	-125	-137	-147	-158
Economic Profit	-17	-24	-26	-9	-40
Discounting Factor	0.99	0.89	0.81	0.73	0.66
Present value of excess equity	-1	-22	-21	-7	-26

Source: FAB Securities

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 1.1x. The Investment Banking Segment is valued using the PE multiple of regional and global peers with a median PE multiple of 12.5x. Treasury and Hold Co. Segment is valued using international peers using a median PB multiple of 0.6x.

Commercial bank	Market (USD Mn)	PB (x)		PE (x)	
		2023F	2024F	2023F	2024F
Bank Muscat	5,395	1.2	1.1	10.7	9.5
RAK Bank	2,908	1.1	1.1	6.1	7.4
Mashreq Bank	8,302	1.2	NA	5.3	5.6
Commercial Bank of Dubai	3,747	1.0	1.0	NA	NA
Bank Aljazira	3,675	1.1	1.0	15.6	13.0
Qatar Islamic Bank	12,010	1.8	1.6	10.8	9.9
Average		1.2x	1.2x	9.7x	9.1x
Median		1.1x	1.1x	10.7x	9.5x
Max		1.2x	1.1x	10.8x	9.9x
Min		1.1x	1.0x	6.1x	7.4x

Source: FAB Securities

Investment bank	Market (USD Mn)	PB (x)		PE (x)	
		2023F	2024F	2023F	2024F
Jefferies Financial Group	7,287	0.8	0.7	28.4	9.2
Stifel Financial Group	6,153	1.3	1.2	13.0	10.7
Guotai Junan Securities	17,410	0.9	0.8	11.4	9.2
Lazard	2,527	6.8	5.3	NA	11.0
EFG Hermes holdings	908	1.2	1.1	12.5	10.7
Lincoln National Corporation	4,067	1.4	1.1	5.7	3.6
Average		2.1x	1.7x	14.2x	9.1x
Median		1.3x	1.1x	12.5x	9.9x
Max		1.4x	1.2x	13.0x	10.7x
Min		1.0x	0.9x	11.4x	9.2x

Source: FAB Securities

Treasury and Holdco	Market (USD Mn)	PB (x)		PE (x)	
		2023F	2024F	2023F	2024F
Nomura Holdings	12,260	0.6	0.5	12.7	11.2
Canaccord Genuity Group	473	1.1	0.8	NA	NA
Barclays PLC	26,840	0.4	0.3	5.0	4.4
PNC financial services	51,620	1.2	1.1	9.7	10.4
Insignia Financial	941	0.6	0.7	NA	22.1
Average		0.8x	0.7x	9.1x	12.0x
Median		0.6x	0.7x	9.7x	10.8x
Max		1.1x	0.8x	11.2x	13.9x
Min		0.6x	0.5x	7.3x	8.9x

Source: FAB Securities

Research Rating Methodology:

Rating	Upside/Downside potential
BUY	Higher than +15%
ACCUMULATE	Between +10% to +15%
HOLD	Lower than +10% to -5%
REDUCE	Between -5% to -15%
SELL	Lower than -15%

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