

Jaap Meijer, MBA, CFA

jaap.meijer@arqaamcapital.com
+971 4 507 1744

Janany Vamadeva

janany.vamadeva@arqaamcapital.com
+ 44 7518 406 347

DFM

Volatility has supported volumes, play on Dubai recovery, albeit already priced in

- Benefits from higher trading volume (+28% y/y) with 9M EPS +26%, yet volume remains 80% below FY 07 peak and -61% vs avg. FY14-17A.
- Trading volumes remain the key driver for DFM unlike Boursa Kuwait which secures c.50% of revenue from recurring subscription fees.
- DFM trades at 32.5x 2021e earnings vs. Boursa Kuwait 18.4x, at the higher end of exchange universe, discounting improving prospects for Dubai – UAE family laws, re-opening –, IPO potential, high bottom-up upside in DFM constituencies (30%) and strong cash position (53% of market cap and net cash at 29.8%).
- Catalyst: Potential M&A with ADX, offering synergies (up to 50% in costs).

Market volatility helped earnings growth YTD. Traded value increased 5.2% sequentially in Q1 20, 18.5% in Q2 and 15.8% in Q3, with 9M 20 +28.3% y/y as elevated market volatility supported volumes, with equally strong volumes expected in Q4e, despite lack of index events on DFM as seen in other GCC markets, with the market benefitting from a rotation into re-opening stocks. Earnings increased 25.8% during 9M 20, mainly driven by increase of 29.2% in trading fees.

DFM well positioned for a re-opening trade, with 30% upside from our covered universe. The UAE has drastically reformed its family laws effective as of this week. The improvements affect laws that relate to divorce and separation, how wills and assets are divided, alcohol, suicide, the protection of women, and unmarried people. Dubai is also likely to disproportionately benefit from re-opening following the roll out of vaccines, given the high exposure to tourism, entertainment and logistics sectors, with DFM listed stocks such as EMAAR (8.5% of MC, 11.6% of VOL), EMAARDEV (3.9%, 3.6%), EMAARMLS (8.9%, 4.6%) and AIRA (2.2%, 2.7%) highly geared for a recovery, and ENBD (25.7%, 23.1%) well positioned for a normalization in interest rates, and DIB (12.5%, 8.5%) geared for a FOL increase to 40%, probably by Q1 21e.

Earnings are highly geared for improved trading volumes. Key underlying driver remains the business model, which mainly relies on trading volumes, with a high operating leverage. We increase the target market cap for FY 21e as we turn more bullish on Dubai. We forecast average daily traded value to improve to USD 81.3m in 2020e from USD 60.8m in 2019 and reach USD 153.9m by 2024e, still c.60% below the peak seen in 2007 and 5% below the average of 2014-19. We expect the churn ratio to improve during our forecast horizon, reaching 21% by 2024e from 18% in 2020e. Trading fees and clearing settlement/depositary fees constitute c.60% of revenue, whilst investment income 32%, which should remain pressured due to the low interest rate environment. We expect DFM's C/I to improve from 62% in FY 19A and hit 43.8% in FY 23e.

Boursa Kuwait offers a less volatile revenue base, and a strong Q4e, though the index offers less long-term upside. Boursa Kuwait, which derives little north of half of its revenue from steady stream of annual subscription fees driven by market cap and c.40% from trading fees, generating RoE in the region of 30% (vs 2-3% for DFM reflecting high intangibles), and is a play on index flows in Q4e, with Kuwait attracting USD 2.5bn of inflows from index trackers. However, we see less upside in the underlying constituencies of its index, with the index having run up ahead of the index upgrade by MSCI slated for Nov 30/1Dec 1.

Maintain Hold, at 5% premium on EV/EBITDA and 130% on P/E vs Boursa Kuwait. DFM is currently trading at 32.5x 2021e earnings, 25.6x cash earnings (adjusted for depreciation) versus 5YR EPS CAGR 2019-24e of 19.6% and RoE 20-22e of 2.0-2.9%, looking stretched (trading at the top end of its peers closer to LSE 78.4x vs. RoE of 16% and Hong Kong SE 51.8x vs. RoE of 20.6%), however, still cheap in historical context. Given strong cash balance, on EV/EBITDA, DFM is trading at a multiple of 13.3x (16.6x on net cash) vs. 12.6x (13.0x on net cash) for BOURSA. We prefer to play the re-opening of the UAE through EMAAR, EMAARMLS, AIRA, DU, ENBD and ARMX instead of DFM, while also preferring Boursa Kuwait in the near term (proxy play on index inclusion of Kuwait end Nov/early Dec).

M&A a positive catalyst, but limited progress so far. ADX has converted into a public joint company, which could be read as a step towards the long-awaited merger between DFM and ADX, though we have not seen any progress on that front so far. The gap between ADX and DFM has narrowed with ADX traded value now representing 81% of DFM (9M 20) vs. 75% in 2011 and 37% in 2016. A merger with ADX would almost double traded value for DFM, with cost synergies (we estimate c.50% of the combined cost base), making it a compelling case for shareholders, boosting recurring EPS by c.50%.

HOLD

AED 0.83

Banks / UAE

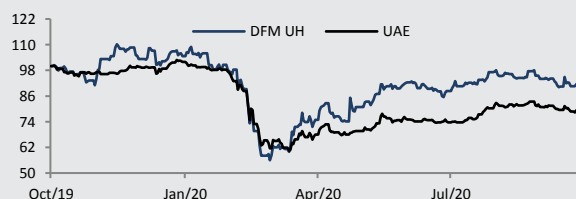
Bloomberg code	DFM UH
Market index	UAE
Target Price	0.83
Upside (%)	-2.0

Market data 11/10/2020

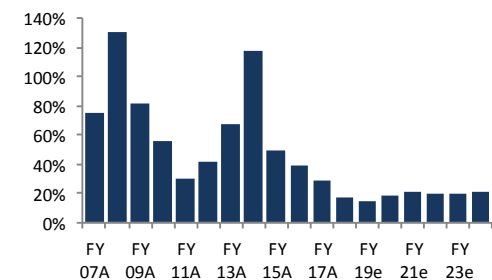
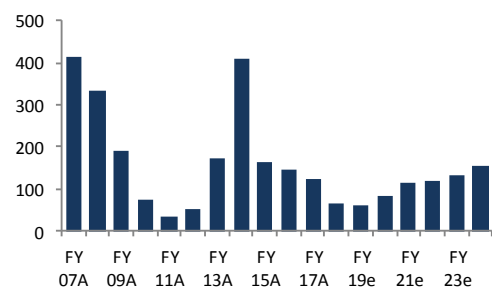
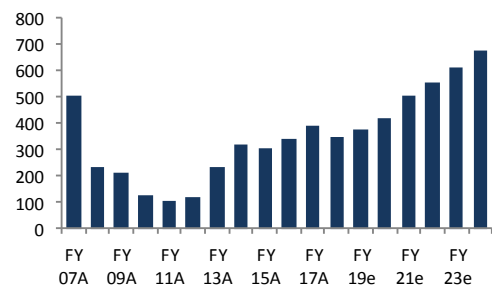
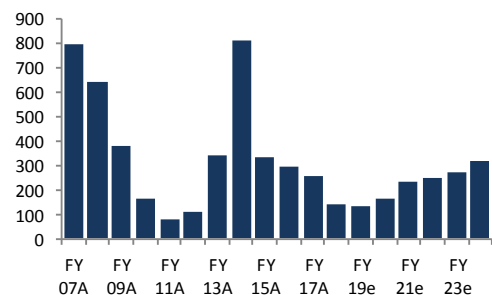
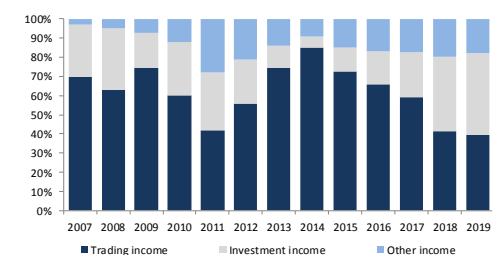
Last closing price	0.85
52 Week range	0.5-1.0
Market cap (AED m)	6,784
Market cap (USD m)	1,847
Average Daily Traded Value (AED m)	5.0
Average Daily Traded Value (USD m)	1.3
Free float (%)	19%

Year-end (local m)	2018	2019	2020e	2021e
Revenues	333	324	365	416
Pre-provisioning profit	126	122	162	211
EPS	0.02	0.02	0.02	0.03
P/E (x) (mkt price)	54.2	56.3	42.4	32.5
BVPS	1.0	1.0	1.0	1.0
Tangible BVPS	0.3	0.4	0.4	0.4
P/B (x) (mkt price)	0.9	0.9	0.9	0.9
P/TBVPS (x) (mkt price)	2.5	2.3	2.3	2.3
DPS	-	0.03	0.02	0.02
Div. yield (%)	-	2.9	1.8	2.3
RoAA (%)	1.3	1.3	1.6	2.1
RoRWA (%)	1.9	1.7	2.1	2.7
RoATE (%)	1.6	1.5	2.0	2.6
Number of shares	7,996	7,996	7,996	7,996

Price Performance



Abacus Arqaam Capital Fundamental Data

DFM churn ratio

DFM ADTV USD m

DFM index market capitalization USD bn

Fee income AED m

Revenue composition

DFM

Year-end	2018	2019	2020e	2021e	2022e	2023e
Performance analysis						
Cost / Income (%)	62.3	62.3	55.6	49.2	47.1	43.8
Fees & Commissions / operating income (%)	41.5	39.9	45.3	56.1	55.9	57.0
Trading gains / operating income (%)	39.0	43.3	31.4	22.3	22.6	22.0
RoATE (%)	1.6	1.5	2.0	2.6	2.9	2.9
RoAA (%)	1.3	1.3	1.6	2.1	2.2	2.3
Year-end	2018	2019	2020e	2021e	2022e	2023e
Growth						
Revenues (%)	(22.5)	(2.9)	12.9	13.7	5.4	8.2
Cost (%)	5.8	(3.0)	0.9	0.5	0.9	0.5
Net Profit (%)	(46.1)	(3.9)	33.0	30.3	9.7	3.5
Assets (%)	0.2	2.5	2.8	2.5	2.0	2.0

Abacus Arqaam Capital Fundamental Data

Company Profile

Dubai Financial Market was established in 2000 as a secondary market for trading securities issued by public joint-stock companies, bonds issued by the Federal Government or any of the Local governments and public institutions. Borse Dubai owns 80% of DFM and the remainder is free float.

Key drivers

- Upside from our TPs for DFM listed stocks
- Increase in FOL
- New IPOs increasing market cap, boosting mostly secondary trading volumes along with one-time listing fee of AED 50k
- Rising interest in the region by institutional investors leading to churn ratios (currently foreign investors account for 51% of trading and institutional investors 53%)
- DFM charges 20 bps per trade (from both sides of the trade – buyer and seller)
- Successful launch of Sukuk trading platform with widespread acceptance and use
- Lower rate environment should weigh on interest/investment income given huge cash and equivalent balance of AED 3.6bn, 36% of total assets
- Investment in headquarters worth around USD 200m to be completed in 2-3 years at Business Bay (land gifted by Dubai Properties Group)
- Market cap to GDP of 61% for the UAE offers further room to grow

DFM

Year-end	2018	2019	2020e	2021e	2022e	2023e
Income statement (AED m)						
Fee income	138	129	165	233	245	270
Net investment income	130	140	115	93	99	104
Other operating income	66	58	87	91	96	100
Total operating income	333	324	365	416	438	474
Total operating expenses	208	202	203	204	206	207
Pre-provision operating profit	126	122	162	211	232	266
Other provisions / impairment	-	-	-	-	-	-
Operating profit	126	122	162	211	232	266
Associates	-	-	-	-	-	-
Pre-tax profit	126	122	162	211	232	266
Taxation	-	-	-	-	-	27
Net profit	126	122	162	211	232	240
Attributable net profit	125	121	160	209	229	237
Diluted EPS	0.02	0.02	0.02	0.03	0.03	0.03
DPS	-	0.03	0.02	0.02	0.02	0.02
BVPS	0.97	0.98	0.99	1.00	1.00	1.01
Tangible BVPS	0.34	0.36	0.37	0.37	0.38	0.39

Year-end	2018	2019	2020e	2021e	2022e	2023e
Balance sheet (AED m)						
Cash and central bank	3,111	3,258	3,466	3,727	3,951	4,178
Investment, net	1,012	1,110	1,179	1,206	1,228	1,251
Fixed assets, net	294	345	339	299	256	214
Other assets	5,025	4,969	4,969	4,969	4,969	4,969
Total assets	9,443	9,681	9,952	10,201	10,405	10,613
Debt	28	29	29	29	29	29
Other liabilities	1,631	1,760	2,002	2,198	2,345	2,493
Total liabilities	1,659	1,790	2,031	2,227	2,374	2,522
Total equity	7,783	7,891	7,921	7,973	8,031	8,090

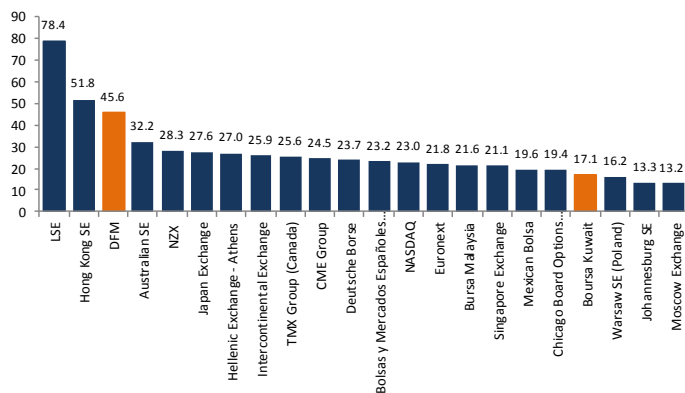
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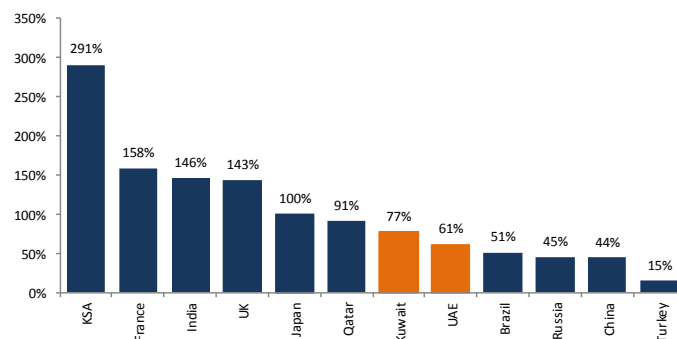
Arqaam Capital Research Offshore s.a.l

Exhibit 1: P/E (x): DFM continues to trade at a higher multiple, especially, vs. regional peer, BOURSA KK



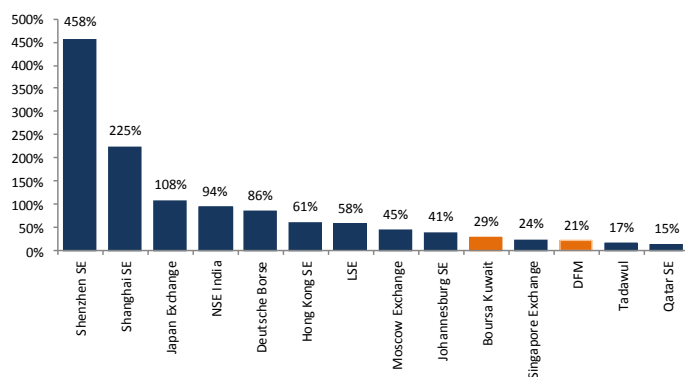
Source: Bloomberg, Arqaam Capital Research

Exhibit 2: Market cap to GDP: IPO potential offers lot of scope to boost volumes



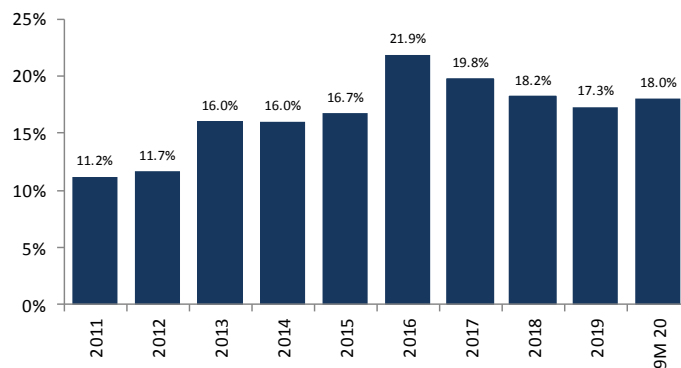
Source: Company Data, IMF, Stock Exchanges, Arqaam Capital Research

Exhibit 3: Churn ratio: In line with the region



Source: Company data, Arqaam Capital Research

Exhibit 4: Foreign ownership % of market capitalization



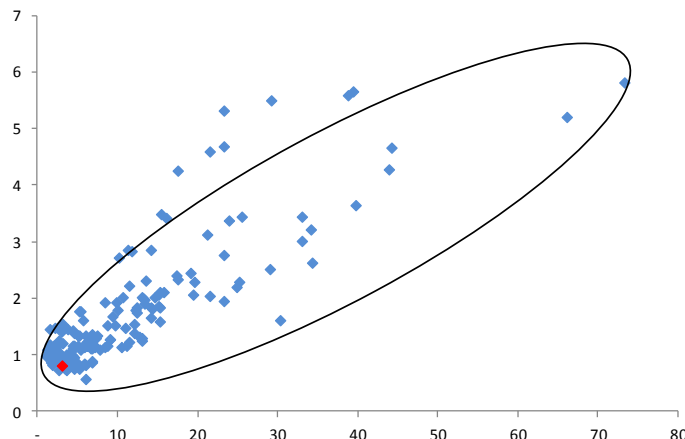
Source: Company Data, Arqaam Capital Research

Exhibit 5: DFM share price vs. DFMGI Index

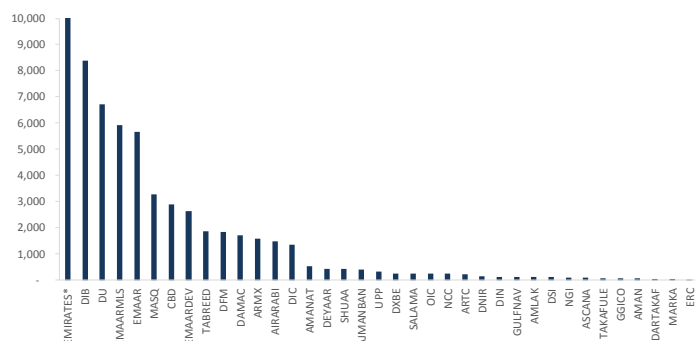


Source: Company Data, Arqaam Capital Research

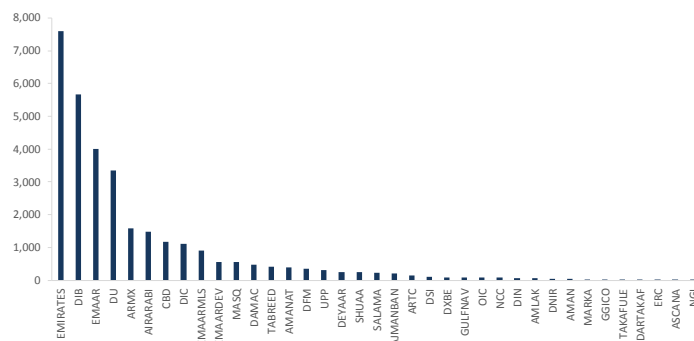
Exhibit 6: Traded value (X-axis AED bn) vs. DFM price (AED)



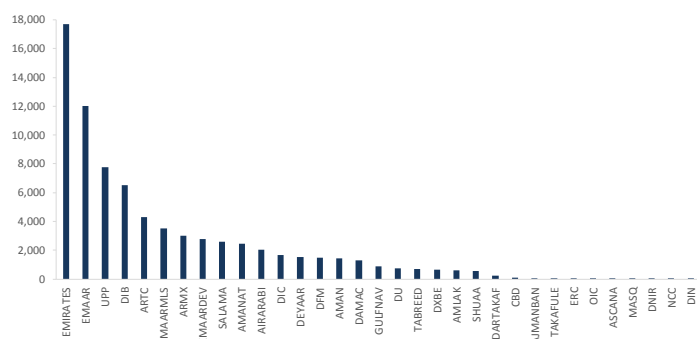
Source: Company Data, Arqaam Capital Research

Exhibit 7: Market Cap


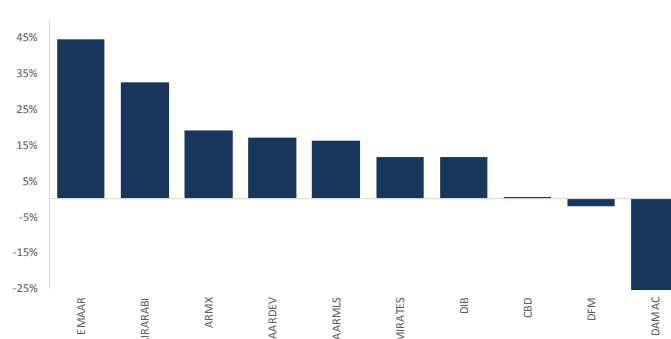
Source: Company Data, Arqaam Capital Research

Exhibit 8: Free Float Market Cap


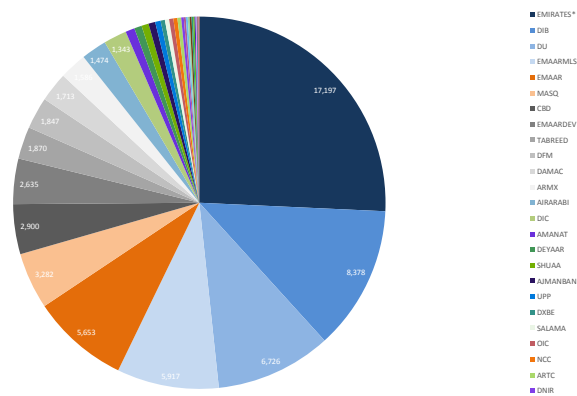
Source: Company Data, Arqaam Capital Research

Exhibit 9: Daily Traded Value


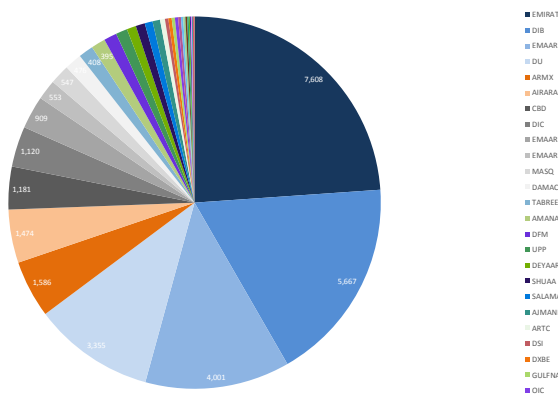
Source: Company Data, Arqaam Capital Research

Exhibit 10: Upside


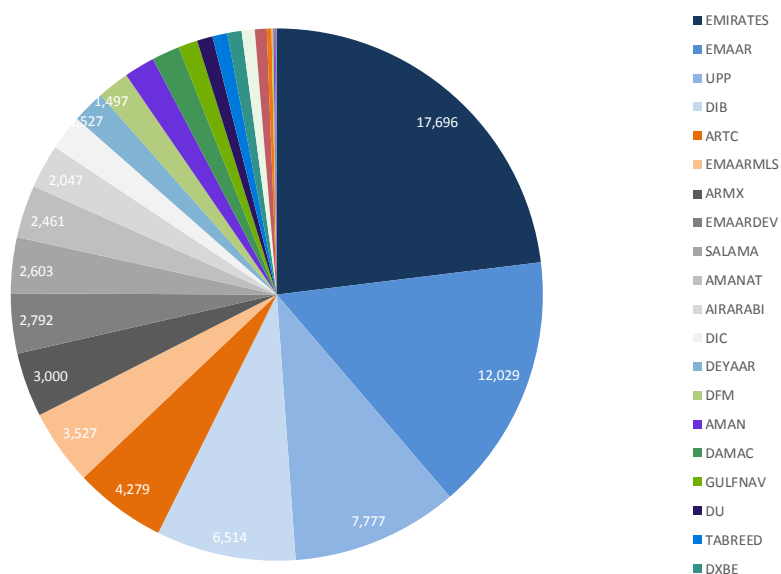
Source: Company Data, Arqaam Capital Research

Exhibit 11: Market Cap


Source: Company Data, Arqaam Capital Research

Exhibit 12: Free Float Market Cap


Source: Company Data, Arqaam Capital Research

Exhibit 13: Daily Traded Value


Source: Company Data, Arqaam Capital Research

Exhibit 14: Valuation comp – DFM's low P/BV explained by intangibles and high cash balance, high P/E partly justified by high cash balances and growth prospects

Ticker	Name	Mkt Cap AED m	P/E (x)	RoE (%)	Dvd 12M Yield (%)	P/B (x)
MOEX RM Equity	Moscow Exchange	15,464	13.2	18.6	5.6	2.4
JSE SJ Equity	Johannesburg SE	2,540	13.3	21.5	6.9	2.8
GPW PW Equity	Warsaw SE (Poland)	1,843	16.2	13.5	5.3	2.1
BOURSA KK Equity	Boursa Kuwait	2,822	18.1	35.1	2.2	7.2
CBOE US Equity	CBOE Holdings	33,592	19.4	14.4	1.8	2.7
BOLSAA MM Equity	Mexican Bolsa	5,266	19.6	22.3	3.7	4.2
SGX SP Equity	Singapore Exchange	27,204	21.1	40.6	3.3	8.0
BURSA MK Equity	Bursa Malaysia	6,155	21.6	42.1	3.2	8.7
ENX FP Equity	Euronext	28,448	21.8	37.3	1.7	6.7
NDAQ US Equity	NASDAQ	80,254	23.0	17.0	1.4	3.6
BME SM Equity	Bolsas Y Mercados Espanoles (Spain)	12,030	23.2	29.0	3.1	6.4
DB1 GR Equity	Deutsche Borse	114,144	23.7	20.2	2.1	4.2
CME US Equity	CME Group	198,564	24.5	8.2	3.9	2.0
X CN Equity	TMX Group (Canada)	20,517	25.6	8.0	2.1	2.0
ICE US Equity	Intercontinental Exchange	207,520	25.9	11.9	1.2	3.0
EXAE GA Equity	Hellenic Exchange - Athens	751	27.0	6.0	5.6	1.7
8697 JP Equity	Japan Exchange	47,346	27.6	17.3	2.2	4.6
NZX NZ Equity	NZX	1,271	28.3	27.0	3.4	7.7
ASX AU Equity	Australian SE	43,172	32.2	13.3	2.9	4.3
DFM UH Equity	DUBAI FINANCIAL MARKET	6,624	45.6	1.9	3.0	0.9
388 HK Equity	Hong Kong SE	232,928	51.8	20.6	1.7	10.4
LSE LN Equity	LSE	151,456	78.4	16.2	0.8	8.4

Source: Arqaam Capital Research, Bloomberg

Exhibit 15: DFM valuation (AED m)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020e	2021e	2022e	2023e	2024e	perp	subtotal	% of total
1. DCF																		
Net profit	79	-7	35	285	759	261	253	233	125	121	160	209	229	237	295	310		
Other adjustments	76	76	76	76	76	77	78	79	79	79	79	79	79	79	79	79	83	
Minus: excess return excess capital	32	33	36	43	52	45	42	46	40	42	42	42	43	44	45	47		
Risk free rate	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%		
Tax shelter	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%		
Adjusted net profit	123	36	75	318	784	292	289	266	164	158	198	246	265	272	329	345		
Capital requirements	451	405	344	510	616	599	702	794	785	853	908	931	951	971	991	1,040		
RoEC	27.3%	8.8%	21.9%	62.3%	127.2%	48.8%	41.2%	33.4%	20.9%	18.5%	21.8%	26.4%	27.9%	28.1%	33.2%	33.2%		
Cost of capital	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%		
Capital charge	45	40	34	51	62	60	70	79	78	85	91	93	95	97	99	104		
Economic profit	78	-5	41	267	722	232	219	186	86	72	107	153	170	175	230	241		
Discount factor	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	1.000	0.909	0.826	0.751	0.683	0.621		
NPV of Economic Profit	0	0		0	0	0	0	0	0	0	107	139	141	132	157	241		
DCF EVA Forecast period																	675	10.1%
Perpetual growth rate (nominal GDP)																	5.0%	
Terminal Value																	4,826	
Terminal value discounted																	2,996	45.0%
Required Capital																	908	13.6%
Value of the investment banking operations																	4,579	68.8%
2. Capital surplus/deficit																		
Available capital:																		
Shareholders equity 2010	7,523	7,479	7,458	7,935	8,413	8,028	7,902	8,142	7,764	7,871	7,911	7,963	8,020	8,080	8,154			
Minorities	43	43	43	43	43	44	45	46	46	46	46	46	46	46	46			
Less Goodwill & intangibles	-5,526	-5,450	-5,374	-5,326	-5,263	-5,201	-5,138	-5,082	-5,025	-4,969	-4,969	-4,969	-4,969	-4,969	-4,969			
Less non equity elements																		
Less dividends	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Tangible equity	2,040	2,072	2,126	2,653	3,193	2,871	2,808	3,106	2,785	2,948	2,988	3,040	3,098	3,157	3,231			
Capital needs																		
RWAs	3,754	3,373	2,869	4,250	5,134	4,993	5,850	6,619	6,540	7,108	7,564	7,761	7,923	8,088	8,256			
RWAs (Basel 3)	3,754	3,373	2,869	4,250	5,134	4,993	5,850	6,619	6,540	7,108	7,564	7,761	7,923	8,088	8,256			
Equity as % RWA	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%			
Financial stakes	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0			
Capital Requirements	451	405	344	510	616	599	702	794	785	853	908	931	951	971	991			
Surplus capital	1,590	1,667	1,782	2,143	2,577	2,272	2,106	2,311	2,000	2,095	2,080	2,109	2,147	2,186	2,240		2,080	31.2%
3. Other adjustments																		
Real estate losses																	0	
Equity investment losses																	0	
Level 3 assets																	0	0.0%
4. Dividends																	0	0.0%
Total Fair Value																	6,659	100%
Number of shares																	7,996	
Fair value per share																	0.83	
Current share price																	0.85	
Upside																	(2.0%)	
Implied P/E								28.6x	53.1x	55.2x	41.5x	31.9x	29.0x	28.1x	22.6x			
Implied P/B								2.2x	2.4x	2.3x	2.3x	2.2x	2.2x	2.1x	2.1x			

Source: Company Data, Arqaam Capital Research

Changes to UAE family law and immigration policies

The UAE modernizes the legal system, with changes to family laws, effective immediately, reflecting progressive measures to improve living standards, further supporting the UAE as a destination for FDIs and expats. The reforms affect laws that relate to divorce and separation, how wills and assets are divided, alcohol, suicide, and the protection of women, amongst others. Expats can deal with personal affairs according to the laws of their home country. The changes mean that the laws of a person's country of origin can be used for divorces and inheritance, and Islamic law would be rarely used when it comes to family law cases involving expatriates, as citizenships will now dictate how assets are divided instead of adjudicating to the Shariah law, except for UAE property.

Alcohol consumption is no longer a criminal offense. Anyone who drinks or is in possession of alcohol or sells alcoholic beverages in authorised areas without an alcohol license will not face penalties.

Suicide and attempted suicide will be decriminalized, though anyone found assisting an individual with an attempted suicide will face a jail sentence, while those who intervene in situations where people are in need cannot be held liable for the outcome of those they help, as fear of prosecution had stopped residents from learning life-saving first aid in UAE.

Rights of women improved: There will no longer be a distinction of crimes known as "honor crimes", where a male relative can get a lighter sentence for assaulting a female relative under the guise of "protecting honor", and tougher punishments for men who subject women to harassment of any kind, including street harassment or stalking.

The new changes in the legal system follow a series of relaxed visa rules including retirement in Dubai for >55-aged qualified expatriates, who have a monthly income of AED 20k, or cash savings of AED 1m, or own property >AED 2m, or have a combination of options 2 and 3 valued >AED 2m. Other new relaxed visa benefits in Dubai include eligibility for a 3-year visa for investors owning property >AED 1m, 5-year visa if property >AED 5m, and 10-year visa for investments >AED 10m of which 40% in real estate.

Dubai also recently liberalized its immigration policies for WFH foreign professionals, for those that have jobs or own companies abroad, earning > USD 5k/month, allowing them to benefit from zero income tax in the UAE.

Exhibit 16: New Law Amendments, the UAE becoming more modern and secular

Divorce & Inheritance

The laws of the country where the marriage took place will apply in the case of a divorce

The court can be called on to mediate an agreement for joint assets and accounts

A person's citizenship will dictate how their assets are divided, unless they have a will written

Suicide

Suicide and attempted suicide will be decriminalized

Courts and police will ensure people receive mental health support

"Good Samaritans" cannot be held accountable for the outcome of those they help

Those found assisting with an attempted suicide will face time in jail

Harassment and assault

There will no longer be any distinction between crimes and "honor crimes"

Tougher punishments will be applied on men who subject women to harassment of any kind

The punishment of the rape on a minor or someone with limited mental capacity will be execution

Alcohol Consumption

Consumption of alcohol will no longer be a criminal offense

Selling, consumption and drinking of alcohol in authorized areas will not face any penalties

Individuals must be at least 21 years old to drink legally

Cohabitation

Unmarried couples will be allowed to live together

Consensus sex for adults is no longer prohibited

Judicial Procedure Translators will be provided for defendants and witnesses that do not speak Arabic

A privacy law will ensure that evidence related to cases will be protected and not publicly disclosed

Source: News Source, Arqaam Capital Research

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