Company Update

November 30 2023

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GFH Financial Group

Strong IB continues to drive EPS

BUY **USD 0.38/ AED 1.43/ Kwd 120**

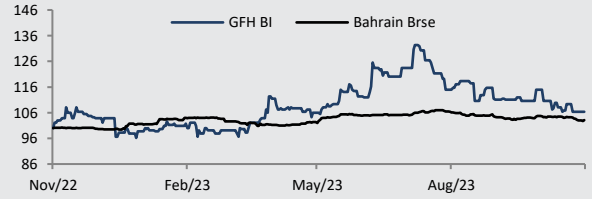
Banks / BAHRAIN

Bloomberg code	GFH BI/ GFH UH/ GFH KK
Market index	Bahrain Brse/ DFM/ Boursa Kuwait
Target Price	USD 0.38/ AED 1.43/ Kwd 120
Upside (%)	55.4%

Market data	**11/14/2023**
Last closing price	USD 0.25/ AED 0.92/ Kwd 77
52 Week range	0.2-0.3
Market cap (USD m)	958
Free float (%)	92%

Year-end (local m)	**2021**	**2022**	**2023e**	**2024e**
Revenue	262	237	264	305
Pre-provisioning profit	128	89	104	142
EPS	0.02	0.02	0.03	0.04
P/E (x) (mkt price)	11.4	10.6	8.9	7.1
BVPS	0.3	0.3	0.3	0.3
Tangible BVPS	0.3	0.3	0.3	0.3
P/B (x) (mkt price)	1.0	1.0	0.9	0.9
P/TBVPS (x) (mkt price)	1.0	1.0	0.9	0.9
DPS	0.01	0.02	0.02	0.02
Div. yield (%)	4.8	6.4	6.4	7.2
RoAA (%)	1.1	1.0	1.1	1.2
RoRWA (%)	1.0	1.2	1.4	1.7
RoATE (%)	9.0	9.2	10.5	12.5
RoEcC (%)	8.0	9.7	11.0	13.5
RAROC (%)	8.7	9.4	10.9	13.5
Net LtD ratio (%)	87.9	106.7	43.1	47.9
Risk Weighted Assets (bn)	8.3	7.3	7.7	7.8
Core Equity T1 ratio (%)	12.1	13.9	15.1	15.8
Tier 1 capital ratio (%)	12.9	14.0	15.2	15.8
Total capital ratio (%)	13.5	14.7	15.8	16.5
NPL ratio (%)	7.1	3.5	8.0	8.0
Coverage ratio (%)	73.2	124.4	52.4	53.4
Number of shares	3,833	3,833	3,833	3,833

Price Performance



- **We leave our forecasts estimates unchanged, penciling in an EPS growth of 18.9% for FY23e and an EPS CAGR of 15.6% for FY 23-27e, with RoE expanding from 10.5% in FY23 to 14.0% in FY 27e.**
- **In Q3, the strong performance was supported by deal flow for the IB division, despite surging OpEx and finance expenses. EPS increased by only 1.0% y/y in Q3, as stronger IB performance (2.7x) was offset by i) weaker commercial banking and treasury/proprietary investments (-68% combined) impacted by higher finance expense and ii) higher OpEx. As a result, 9M EPS growth reached 20% y/y (USD 2.26).**
- **Balance sheet expanded by 8% YtD driven by a continuous surge in deposits (140% YtD), which was largely allocated to the treasury book.**
- **Maintain BUY as the current valuation at 0.9x P/BV is not pricing in better earnings resilience, RoE expansion, and growing AuM base.**

We pencil in an EPS CAGR of 10% for FY23-27e, with RoE expanding from 9% in FY22 to 14% for FY27e. The IB division continues to bolster GFH's performance, especially following Q3 surge (1.7x q/q), though was mostly offset by higher-than-expected OpEx and finance expenses, up by 71% and 25% y/y, respectively. Impairment increased as well by 109% y/y, mainly due to the treasury portfolio. The IB performance was supported by several transactions during Q3 23, including the placement of Saudi Food Logistics, US Opportunistic Fund, US Logistics II, and Student Housing III. As a result, EPS growth was limited to 1% y/y (-21% q/q), lifting 9M EPS by 20% to USD 2.26.

Ambitious targets. GFH plans to grow its asset base and AUM to USD25bn by YE 25e through i) organic growth, via creating strategic PE platforms (i.e., GFH's education investment arm Britus Education) and ii) inorganic growth, via acquiring strategic businesses (i.e., acquisition of Asset Managers to strengthen footprint in the UK, and US). We expect a revenue CAGR FY23-27e of 10.7%, operating profit CAGR of 20.3%, and EPS CAGR of 15.6%, with RoE gradually improving from 9.2% in FY22 to 14.0% in FY27e and RoRWA improving from 1.2% in FY22 to 2.1% in FY27e. While it remains dependent on transactional gains for a significant share of its revenues, however, we see those gains as recurring.

De-risked strategy. GFH cut its real estate portfolio (23.6% of assets in FY 21 to 12.6% in Q2 23A). The group plans to improve return generation by enhancing existing business lines through ii) refocusing on financial assets across the rest of the group, iii) enhancing Khaleeji's asset base, iv) expanding treasury operations and investment banking, and v) expanding international footprint.

Expanding asset base supported by a growing deposit base allocated mainly to the treasury portfolio. Asset growth was 8.0% YtD, mainly through higher investments in the treasury portfolio (+18%) and loan book (+9%), funded mainly by an expansion in equity of investment account holders, up by 142% YtD (mainly through financial institution funding). As of Q3, net-debt-to-equity ratio stands at 0.62x vs. 1.09x at YE 22A. GFH targets to grow the AuM base from USD 18.8bn to USD 25bn through organic/inorganic growth.

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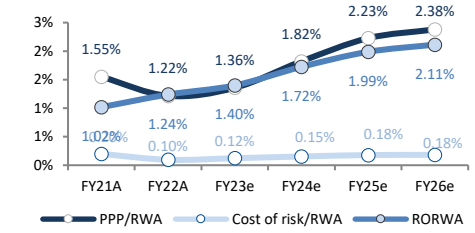
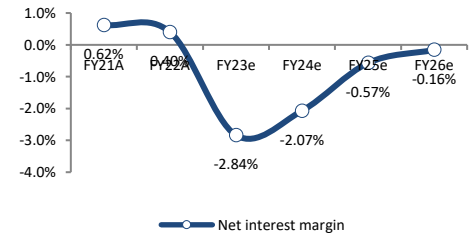
Abacus *Arqaam Capital Fundamental Data*

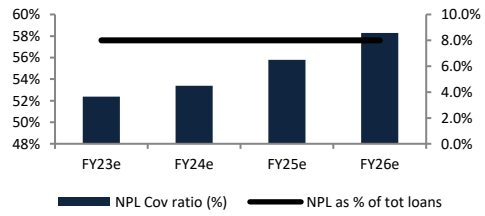
Profitability



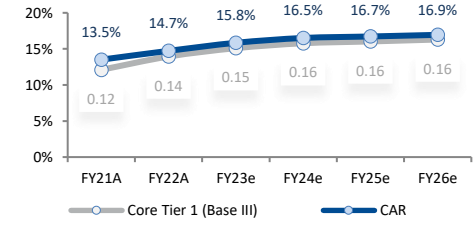
NIM



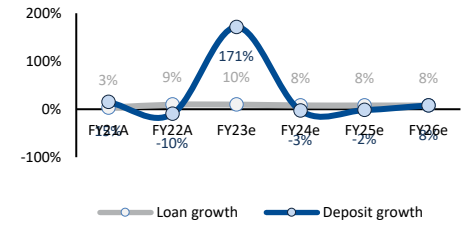
Credit Quality



Capital Ratios



Growth



GFH Financial Group

Year-end	2021	2022	2023e	2024e	2025e	2026e
Performance analysis						
Net Interest Margin (%)	0.62	0.40	(2.84)	(2.07)	(0.57)	(0.16)
Asset yield (%)	4.13	4.38	5.20	5.20	4.30	4.30
Cost of Funds (%)	1.44	1.38	2.33	2.35	1.90	1.80
Risk Adjusted Margins (%)	(0.23)	0.08	(3.28)	(2.53)	(1.00)	(0.58)
Cost / Income (%)	51.0	62.5	60.5	53.4	47.7	45.2
Net Interest Income / total income (%)	4.6	3.7	(23.1)	(17.7)	(5.5)	(1.6)
Fees & Commissions / operating income (%)	1.8	3.9	10.5	10.0	9.5	9.6
Trading gains / operating income (%)	62.9	75.1	97.1	92.9	81.9	77.7
RoATE (%)	9.0	9.2	10.5	12.5	14.1	14.7
Pre-prov. RoATE (%)	10.4	9.8	11.2	13.1	14.8	15.3
RoAA (%)	1.1	1.0	1.1	1.2	1.4	1.4
Revenue / RWA (%)	3.17	3.25	3.44	3.91	4.25	4.35
Costs / RWA (%)	1.62	2.03	2.08	2.09	2.03	1.96
PPP / RWA (%)	1.55	1.22	1.36	1.82	2.23	2.38
Cost of Risk / RWA (%)	0.20	0.10	0.12	0.15	0.18	0.18
RoRWA (%)	1.02	1.24	1.40	1.72	1.99	2.11
RoRWA (%) (adj. for gross-up of associates)	1.02	1.24	1.40	1.72	1.99	2.11

Year-end	2021	2022	2023e	2024e	2025e	2026e
Asset Quality						
Provisions charge / avg. gross loans (%)	1.2	0.5	0.6	0.7	0.8	0.8
Past due not impaired / gross loans (%)	4.1	4.8	3.9	3.9	4.0	4.1
NPL / gross loans (%)	7.1	3.5	8.0	8.0	8.0	8.0
NPL coverage ratio (%)	73.2	124.4	52.4	53.4	55.8	58.3
Provisions / avg. gross loans (%)	4.1	4.8	3.9	3.9	4.0	4.1
Provisions charge / operating income (%)	12.8	7.8	9.1	8.4	8.0	7.6

Year-end	2021	2022	2023e	2024e	2025e	2026e
Funding and Liquidity						
Net Loans / Deposits (%)	87.9	106.7	43.1	47.9	52.5	52.4
Cash and interbank / assets (%)	8.9	8.8	4.0	6.7	2.4	1.0
Deposits / liabilities (%)	21.6	15.5	38.4	34.5	31.4	31.4

Year-end	2021	2022	2023e	2024e	2025e	2026e
Capital and leverage ratios						
Core Tier 1 ratio (Basel III) (%)	12.1	13.9	15.1	15.8	16.0	16.3
Tier 1 ratio (%)	12.9	14.0	15.2	15.8	16.1	16.3
Total capital ratio (%)	13.5	14.7	15.8	16.5	16.7	16.9
Tangible equity / assets (%)	14.5	11.0	10.6	10.5	10.6	10.6
RWA / assets (%)	102.3	74.6	72.1	67.9	66.7	65.6

Year-end	2021	2022	2023e	2024e	2025e	2026e
Growth						
Revenues (%)	38.9	(9.6)	11.5	15.8	15.4	8.5
Cost (%)	18.9	10.8	7.9	2.2	2.9	2.9
Pre-Provision Operating Profit Growth (%)	68.4	(30.9)	17.5	36.6	29.7	13.6
Provisions (%)	78.8	(57.7)	35.9	26.8	23.4	8.0
Net Profit (%)	86.8	7.2	18.9	25.4	22.3	12.9
Assets (%)	22.7	20.7	9.0	8.0	8.0	8.0
Loans (%)	3.5	9.5	9.6	7.9	7.8	7.8
Deposits (%)	14.9	(9.8)	171.3	(2.8)	(1.8)	8.0
Risk Weighted Assets (%)	-	(11.9)	5.3	1.8	6.1	6.2

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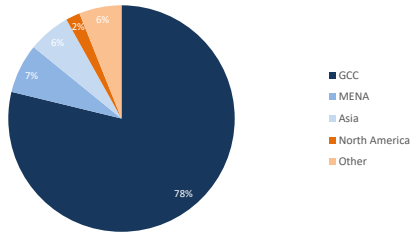
Abacus *Arqaam Capital Fundamental Data*

Company Profile

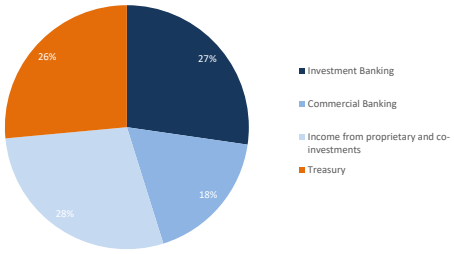
GFH is a Bahrain-domiciled Sharia-compliant financial group that is focused on investment banking, treasury activities, commercial and retail banking in Bahrain via Khaleeji Bank BSC (Khaleeji) and proprietary investments.

S&P raised the credit rating from B- to B with a stable outlook, reflecting the revenue resilience and improvement in RoE.
Infracorp launched a USD 900m green bond on the LSE.
GFH is listed on four stock exchanges.

Geographical breakdown



Revenue Breakdown



**FY 22A*

Management	
CEO	Hisham Ahmed Al Rayes
CFO	Suryanarayanan Hariharan
COO	Salah Abdulla Sharif

Major Shareholders	
Keypoint Trust	7.50%

GFH Financial Group

Year-end	2021	2022	2023e	2024e	2025e	2026e
Income statement (USDmn)						
Interest income	79	95	112	136	146	163
Interest expense	67	86	173	190	166	169
Net Interest Income	**12**	**9**	**(61)**	**(54)**	**(19)**	**(6)**
Fee income	5	9	28	30	33	37
Net investment income	55	58	36	99	96	104
Other operating income	191	161	262	230	242	248
Total operating income	**262**	**237**	**264**	**305**	**352**	**382**
Total operating expenses	134	148	160	163	168	173
Pre-provision operating profit	**128**	**89**	**104**	**142**	**184**	**209**
Net provisions	16	7	9	12	15	16
Other provisions / impairment	19	(4)	12	11	15	16
Operating profit	**93**	**85**	**83**	**119**	**155**	**178**
Associates	-	12	28	20	20	20
Pre-tax profit	**93**	**98**	**111**	**139**	**175**	**198**
Taxation	-	-	-	-	-	-
Net profit	**93**	**98**	**111**	**139**	**175**	**198**
Minorities	8	7	3	4	11	12
Others	-	-	-	-	-	-
Attributable net profit	**84**	**90**	**107**	**135**	**165**	**186**
Diluted EPS	0.02	0.02	0.03	0.04	0.04	0.05
DPS	0.01	0.02	0.02	0.02	0.02	0.02
BVPS	0.25	0.26	0.27	0.29	0.32	0.34
Tangible BVPS	0.25	0.26	0.27	0.29	0.32	0.34

Year-end	2021	2022	2023e	2024e	2025e	2026e
Balance sheet (USDmn)						
Gross loans and advances	**1,382**	**1,500**	**1,642**	**1,773**	**1,915**	**2,069**
Less: loan loss provisions	71	64	69	76	86	96
Net loans and advances	1,311	1,435	1,573	1,698	1,830	1,972
Cash and central bank	722	858	433	1,513	1,763	2,032
Due from banks	-	-	-	-	-	-
Investment, net	5,379	6,644	7,562	7,371	7,853	8,374
Fixed assets, net	140	233	219	219	219	219
Other assets	531	590	851	689	745	804
Total assets	**8,084**	**9,760**	**10,639**	**11,490**	**12,409**	**13,402**
Customer deposits	1,491	1,345	3,649	3,547	3,482	3,761
Due to banks	-	-	6	738	1,467	1,903
Debt	3,863	5,733	4,100	4,100	4,100	4,100
Other liabilities	1,561	1,611	1,756	1,896	2,048	2,212
Total liabilities	**6,916**	**8,689**	**9,511**	**10,281**	**11,097**	**11,976**
Total equity	**1,168**	**1,071**	**1,128**	**1,209**	**1,312**	**1,426**
Risk Weighted Assets (bn)	8	7	8	8	8	9
Average Interest-Earning Assets	1,919	2,163	2,150	2,609	3,402	3,798
Average Interest-Bearing Liabilities	4,691	6,216	7,416	8,070	8,717	9,407
Common shareholders	963	997	1,043	1,117	1,213	1,318
Core Equity Tier 1 (Basel III)	1,001	1,016	1,158	1,231	1,328	1,433
Tier 1 capital	1,064	1,020	1,162	1,236	1,332	1,438

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Surge in stage 2 and 3 loans, though impact remains limited as financing assets make up for 15% of overall assets. Stage 1, 2, and 3 loans make up for 72.0%, 19.4%, and 8.5%, respectively, compared to 85.8%, 9.6%, and 4.6%, at YE 22A. Stage 1, 2, and 3 loans coverage stand at 0.4%, 6.8%, and 29.5%, respectively, compared to 1.4%, 8.4%, and 49.4%, respectively, at YE 22A. The provision deficit widened from USD 7.5m as of YE 22A to 65.5m vs. our standard stress test of 1% coverage on stage 1 loans, 12% on stage 2, and 60% on stage 3. However, the collateral was substantial as of YE 22A, with the average collateral coverage ratio on secured facilities standing at 149.7%. The loan book is well diversified with exposure spread across segments: 31% RE, 24% Others, 15% Manufacturing, 15% Construction, and 14% Trading.

Optimal capital level and liquidity position. GFH operates at optimal capital levels, with T1 and CAR of 14.7% and 15.6%, respectively. Leverage stands at an asset/equity ratio of 10.6x, while net loan/equity is low at 1.6x. GFH reported an NSFR of 106% and an average LCR of 227%. GFH's LT issuer credit rating was raised by S&P Global Ratings to 'B' from 'B-' in FY 22, with a stable outlook.

The current valuation is not pricing in better earnings resilience. The stock trades at 0.9x P/tNAV23e and 9.4x P/E 23e, not recognizing the enhanced focus on RoE, the improved revenue mix, and the limited intangibles on the bank's balance sheet.

Exhibit 1: GFH Q3 23 review table

USD mn	Q3 23A	Q2 23A	q/q 23	Q3 22A	Q2 22A	q/q 22	y/y Q3	y/y Q2	9M 23A	9M 22A	9M y/y
Revenue by segment											
Invst. Banking	75.8	45.4	66.7%	28.6	20.4	40.2%	164.6%	122.5%	166.3	73.7	125.5%
Commercial Banking	6.8	15.8	(56.8%)	21.6	17.1	26.2%	(68.4%)	(7.9%)	48.1	58.5	(17.8%)
Treasury and prop.	5.0	25.6	(80.7%)	15.7	18.6	(15.7%)	(68.4%)	38.0%	47.0	55.9	(15.9%)
Total Revenue	**87.5**	**86.8**	**0.8%**	**65.9**	**56.1**	**17.4%**	**32.8%**	**54.7%**	**261.3**	**188.0**	**39.0%**
Expenses by segment											
Invst. Banking	47.8	29.0	64.9%	19.4	22.3	(13.3%)	147.0%	29.9%	110.3	59.2	86.5%
Commercial Banking	1.5	9.1	(83.2%)	11.7	5.1	130.0%	(87.0%)	78.2%	26.0	28.2	(7.7%)
Treasury and prop.	7.7	9.0	(15.3%)	5.6	5.5	0.5%	38.0%	63.7%	30.3	28.9	4.7%
Total Expenses	**57.0**	**47.1**	**21.0%**	**36.6**	**33.0**	**11.2%**	**55.6%**	**43.0%**	**166.6**	**116.3**	**43.3%**
Impairment allowance	**6.7**	**7.6**	**(12.3%)**	**2.6**	**-1.5**	**(274.4%)**	**nm**	**(611.3%)**	**13.6**	**0.3**	**nm**
Net Income	**23.9**	**32.1**	**(25.7%)**	**26.7**	**24.6**	**8.2%**	**(10.5%)**	**30.3%**	**81.0**	**71.5**	**13.4%**
Assets	**10,542**	**10,336**	**2.0%**	**9,760**	**8,520**	**14.6%**	**8.0%**	**21.3%**	**10,542**	**9,760**	**8.0%**
Liabilities*	**9,464**	**9,284**	**1.9%**	**8,689**	**7,478**	**16.2%**	**8.9%**	**24.2%**	**9,464**	**8,689**	**8.9%**

Source: Company Data, Arqaam Capital Research
**(incl. Equity of Invest. Account holders)*

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Exhibit 2: Valuation Table: (USD m)

Year-end	2016	2017	2018	2019	2020	2021	2022	2023e	2024e	2025e	2026e	2027e	perp	subtotal
1. DCF														
Net profit	217	107	114	66	45	84	90	107	135	165	186	192	197	
Other adjustments (comprehensive income and GW amortization)	--	--	--	--	--	--	--	--	--	--	--	--	--	
Minus: excess return excess capital	18	16	17	10	7	5	5	6	8	10	11	13	13	
Risk free rate	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	
Tax shelter	--	--	--	--	--	--	--	--	--	--	--	--	--	
Adjusted net profit	199	91	97	56	38	79	85	101	126	155	175	179	184	
Capital requirements	516	1,007	964	1,000	993	992	874	920	937	994	1,056	1,122	1,150	
RoEcC	38.5%	9.1%	10.1%	5.6%	3.8%	8.0%	9.7%	11.0%	13.5%	15.6%	16.5%	16.0%	16.0%	
Cost of capital	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	13.0%	
Capital charge	67	131	125	130	129	129	114	120	122	129	137	146	150	
Economic profit	132	(40)	(28)	(74)	(91)	(50)	(29)	(18)	5	26	37	33	34	
Discount factor	--	--	--	--	--	--	--	1.00	0.88	0.78	0.69	0.61	0.54	
NPV of Economic Profit	--	--	--	--	--	--	--	(18)	4	20	26	20	18	
DCF EVA Forecast period														53
Perpetual growth rate (nominal GDP)													2.5%	
Terminal Value													324	
Terminal value discounted														176
Required Capital														874
Value of the bank operations														**1,103**
2. Capital surplus/deficit														
Available capital:														
Shareholders equity	908	1,150	1,059	1,005	913	963	997	1,043	1,117	1,213	1,318	1,422		
Minorities	214	346	364	288	273	205	75	85	92	99	107	116		
Less Goodwill & intangibles	(55)	--	--	--	--	--	--	--	--	--	--	--		
Less non equity elements reported shareholders equity														
Less Dividends (if included in reported equity)	(89)	(85)	(32)	(33)	(18)	(46)	(61)	(61)	(69)	(80)	(88)	(99)		
Tangible equity	978	1,411	1,391	1,260	1,168	1,122	1,010	1,067	1,140	1,232	1,338	1,439		
Capital needs														
RWAs (Basel III)	4,299	8,388	8,031	8,330	8,272	8,268	7,285	7,669	7,805	8,282	8,796	9,352		
Equity as % RWA	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%	12.0%		
Financial stakes	--	--	--	--	--	--	--	--	--	--	--	--		
Capital Requirements	516	1,007	964	1,000	993	992	874	920	937	994	1,056	1,122		
Surplus capital	**462**	**404**	**427**	**260**	**175**	**130**	**136**	**147**	**203**	**238**	**282**	**317**		**136**
3. Other adjustments														
Real Estate hidden value														218
Underprovisionning vs. arqaam acid test (conservative)														(66)
Total adjustments														**153**
4. Dividends														**61**
Total Fair Value														**1,452**
Fully diluted number of shares														3,833
Fair value per share														**0.379**
Current share price														**0.25**
Upside														**51.6%**
Implied P/E (x)	6.7	13.5	12.7	22.0	32.2	17.2	16.1	13.5	10.8	8.8	7.8	7.6		
Implied P/tNAV (x)	1.7	1.3	1.4	1.4	1.6	1.5	1.5	1.4	1.3	1.2	1.1	1.0		

Source: Company Data, Arqaam Capital Research

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