KUWAIT FINANCE HOUSE (KFH)

4Q2009 Results - Weaker than Expected; Reiterate Neutral Rating

21 FEBRUARY 2010

KUWAIT | BANKING

Current Price* : KWD 1.18 **Rating: Neutral**
Fair Value (FV): KWD 1.39

• **KFH's 2009 Earnings Fall 24% Y-o-Y, 5% Lower than Our Forecast:** KFH reported FY2009 net attributable income of KWD119 million, a 24% Y-o-Y decline, due to lower property and investment income. Net attributable income of KWD13 million in 4Q2009 fell by 64% Q-o-Q, as provisioning rose from a low base in 3Q2009. KFH posted a net loss before minorities of KWD17 million in 4Q2009, with a positive minorities contribution leading net attributable profit into positive territory. The bank's FY2009 earnings were 5% lower than expected, with 4Q2009's result missing our forecast by 33% on lower-than-expected investment income. KFH's board proposed a dividend of KWD0.025/share (down from KWD0.04/share in 2008), and issuance of bonus shares of 8% of the bank's paid-in capital.

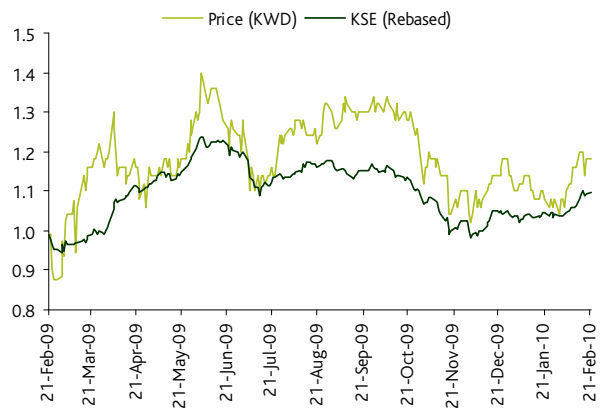
• **NPLs Stable Y-o-Y:** Non-performing financing facilities (in absolute terms) were flat Y-o-Y, following a 488% jump in NPLs during 2008, we believe due to KFH's financing exposure to investment companies in Kuwait, although this has not been confirmed nor clarified by KFH's management. The NPLs outturn in 2009 was better than our expectation of a 30% increase. The coverage ratio stood at 57% in 2009, and has improved from 47% in 2008. When collateral is accounted for, NPLs are more than 100% covered.

• **Investment and Property Income Weak and Lower than Expected in 2009:** Investment and property income fell significantly Y-o-Y and Q-o-Q on lower gains from the sale of available for sale investments and trading properties. Furthermore, KFH posted a net loss from associates and took an impairment charge against its associates during 2009. KFH does not report its share of loss/profit or carrying value per associate, although we believe that the losses stem from KFH's investment associates in Kuwait (Gulf Investment House, First Investment Company, A'ayan Leasing and Investment Company - all reported net losses up to September 2009).

• **Loan Growth Weak, Net Financing Income Expands on Lower Funding Costs:** Net financing facilities grew by 6% Y-o-Y and 1% Q-o-Q, slightly below our expectations. Deposit growth was 10% Y-o-Y and 3% Q-o-Q, helping the bank to lower its borrowings from other banks and financial institutions. Net financing income rose by 7% Y-o-Y, mainly because of a reduction in funding costs. On a Q-o-Q basis, net financing income rose 51% Q-o-Q; however, quarterly financing income growth could be misleading, as KFH only estimates the allocation of profit to depositholders, with the final amount being set after the approval of full-year financial statements.

• **Reiterate Neutral Rating**: The main positive surprise in the results was the stability in NPLs; however, we are not confident that NPLs have peaked, especially considering the large increase in past due, but not impaired, financing facilities (up to 90 days overdue) during 2009. Our forecasts for 2010 assume a recovery in property and investment income, but we see downside risks to our numbers. With the stock trading at rich estimated multiples in 2010 - P/E of 16.7x and P/B of 2.0x, we leave our Neutral rating unchanged.

FLASH NOTE



	2010e	2011e	2012e
EPS	0.071	0.104	0.132
P/E (x)*	16.7	11.4	9.0
DPS	0.028	0.036	0.046
Div Yield (x)	2.4%	3.1%	3.9%
BVPS	0.578	0.646	0.731
P/BV (x)*	2.0	1.8	1.6

In KWD, unless otherwise stated

Stock Data	
Last Dividend Date	*KWD0.04 on 11 Mar 09*
Mkt. Cap / Shares (mn)	*KWD2,720 / 2,305*
Av. Mthly Liqdty (mn)	*KWD121*
52-Week High / Low	*KWD1.40 / 0.875*
Bloomberg / Reuters	*KFIN KK / KFIN.KK*
Est. Free Float	*57%*

*Price as at 21 February 2010

Elena Sánchez- Cabezudo, CFA
+20 2 3332 1145
esanchez@efg-hermes.com

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Figure 1: KFH's 2009 Results, Main Highlights
In KWD million, unless otherwise stated

	2008	2009a	2009e	Y-o-Y	3Q09	4Q09a	4Q09e	Q-o-Q	Vs. Est.
Financing Income	561	528	535	-6%	131	126	133	-4%	-5%
Funding Costs	(298)	(247)	(282)	-17%	(69)	(32)	(67)	-53%	-52%
Net Interest Income	**263**	**281**	**253**	**7%**	**63**	**94**	**66**	**51%**	**42%**
Net Fees & Commissions	70	63	62	-10%	16	16	15	2%	11%
FX Income	14	(2)	8		3	2	12	-45%	-87%
Investment & Property Income	210	112	229	-47%	33	(27)	90		
Other Income	30	66	55	118%	10	29	19	189%	56%
Non-interest Income	**324**	**238**	**354**	**-26%**	**61**	**20**	**135**	**-68%**	**-85%**
Total Banking Income	**587**	**520**	**607**	**-11%**	**124**	**114**	**202**	**-8%**	**-43%**
Operating Expenses	(196)	(239)	(266)	22%	(59)	(64)	(91)	9%	-30%
Operating Profit	**391**	**281**	**341**	**-28%**	**65**	**50**	**111**	**-23%**	**-55%**
Total Provisions	(211)	(204)	(199)	-3%	(35)	(67)	(62)	90%	8%
Extraordinary & Other	-	-	-		-	-	-		
Profit before Tax	**180**	**77**	**142**	**-57%**	**30**	**(17)**	**49**	**-155%**	**-134%**
Taxes & Zakat	(5)	(5)	(5)		(1)	(0)	(0)		
Net Profit	**175**	**72**	**137**	**-59%**	**29**	**(17)**	**49**	**-158%**	**-135%**
Minorities	(18)	47	(12)		5	29	(30)		
Net Profit after Minorities	**157**	**119**	**125**	**-24%**	**34**	**12**	**19**	**-64%**	**-33%**
Receivables	4,780	5,090	5,191	6%	5,035	5,090	5,191	1%	-2%
Deposits	6,612	7,262	7,074	10%	7,015	7,262	7,074	4%	3%
Total Assets	10,544	11,164	11,111	6%	11,091	11,164	11,111	1%	0%

Source: Kuwait Finance House, EFG Hermes estimates

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EGYPT SALES TEAM

Local call center 16900
Int'l call center +20 2 33 33 94 00
cc-hsb@efg-hermes.com

Head of Western Institutional Sales
Mohamed Ebeid
+20 2 33 32 1054
mebeid@efg-hermes.com

Local Institutional Sales
Amr El Khamissy
+20 2 33 32 1045
amrk@efg-hermes.com

UAE SALES TEAM

call center
+971 4 306 9333
uaerequests@efg-hermes.com

Western Institutional Sales
Julian Bruce
+971 4 363 4092
jbruce@efg-hermes.com

Head of GCC Institutional Sales
Amro Diab
+971 4 363 4086
adiab@efg-hermes.com

Gulf HNW Sales
Chahir Hosni
+971 4 363 4090
chosni@efg-hermes.com

UAE Retail Sales
Reham Tawfik
+971 4 306 9418
rtawfik@efg-hermes.com

KSA SALES TEAM

call center
+800 123 4566
RiyadhCallCenter@efg-hermes.com
RiyadhTraders@efg-hermes.com

Deputy Head of Gulf Sales
Ahmed Sharawy
+9661 279 8677
asharawy@efg-hermes.com

RESEARCH MANAGEMENT

Cairo General + 20 2 33 38 8864
UAE General + 971 4 363 4000
efgresearch@efg-hermes.com

Head of Research
Wael Ziada
+20 2 33 32 1154
wziada@efg-hermes.com

Head of Publ. and Distribution
Rasha Samir
+20 2 33 32 1142
rsamir@efg-hermes.com

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CONTACTS AND STATEMENTS

Background research prepared by EFG Hermes Holding SAE. Report prepared by EFG Hermes Holding SAE (main office), 58 Tahrir Street, Dokki, Egypt 12311, Tel +20 2 33 32 1140 | Fax +20 2 33 36 1536 which has an issued capital of EGP 1,939,320,000.

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