

5 May 2011

Change of recommendation

Hold (from Buy)

Target price

Dh19.99 (from Dh18.78)

Price

Dh18.25

Short term (0-60 days)

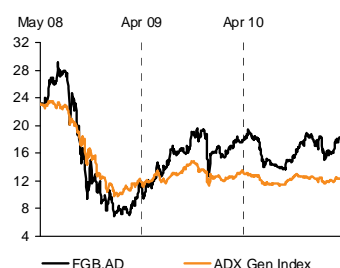
n/a

Market view

No Weighting

Price performance

| | (1M) | (3M) | (12M) |
|----------------|-------|-------|-------|
| Price (Dh) | 16.30 | 17.80 | 18.25 |
| Absolute (%) | 12.0 | 2.5 | 0.0 |
| Rel market (%) | 7.9 | 0.4 | 3.7 |
| Rel sector (%) | 3.6 | -3.8 | -6.2 |



Market capitalisation

Dh27.38bn (€5.02bn)

Average (12M) daily turnover

Dh10.80m (US\$2.99m)

Sector: ADX Bank & Fin Index
 RIC: FGB.AD, FGB.UH
 Priced Dh18.25 at close 4 May 2011.
 Source: Bloomberg

Analyst

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First Gulf Bank

Regulatory hit

FGB is the only bank in the region guiding to a significant regulatory hit from new retail banking regulations. Also, we have concerns about property sector exposure. We view FGB as a quality bank, but there may be better opportunities to buy in 3Q11. We move to Hold with a new Dh19.99 target price (from Dh18.78).

Key forecasts

| | FY09A | FY10A | FY11F | FY12F | FY13F |
|---------------------------|-------|-------|---------|---------|-------|
| Reported PTP (Dhm) | 3,331 | 3,496 | 3,735 ▼ | 4,863 ▼ | 5,732 |
| Reported net profit (Dhm) | 3,310 | 3,420 | 3,776 ▼ | 4,905 ▼ | 5,782 |
| Reported EPS (Dh) | 2.01 | 1.99 | 2.27 ▼ | 3.08 ▼ | 3.65 |
| Normalised EPS (Dh) | 2.06 | 1.99 | 2.27 ▼ | 3.08 ▼ | 3.65 |
| Dividend per share (Dh) | 0.49 | 0.60 | 0.38 ▼ | 0.42 ▼ | 2.78 |
| Normalised PE (x) | 8.85 | 9.18 | 8.05 | 5.93 | 4.99 |
| Price/book value (x) | 1.61 | 1.50 | 1.24 | 1.05 | 1.00 |
| Dividend yield (%) | 2.70 | 3.29 | 2.07 | 2.31 | 15.30 |
| Return on avg equity (%) | 20.20 | 18.50 | 18.30 ▼ | 20.40 ▼ | 21.60 |

Use of ▲ ▼ indicates that the line item has changed by at least 5%.

Accounting standard: IFRS

Source: Company data, Rasmala forecasts

year to Dec, fully diluted

FGB caution leads us to reduce our forecasts

We reduce our GAAP net profit forecast for 2011 by 22% under company guidance, due primarily to caution on the outlook for fee and commission income following the regulatory changes. FGB is linked particularly to personal lending to Nationals, an area we believe is directly addressed by recent regulatory pricing and lending limits.

Provisioning, property and Libyan exposure of more ephemeral concern

Fee and commission income was strong in 1Q11, with the new regulations yet to come into play. Instead, a 39% increase in loan provisioning weighed on the results. However, given this was associated with an increase in the coverage ratio, it likely represents bringing forward some losses to offset future declines in revenue. Property assets remain an area of downside risk given our house view of a falling property market, with a 10% decline in prices equivalent to Dh960m – 4% of market capitalisation, or 5% of book value. Meanwhile, it is an awkward time to have Libyan exposure (via First Gulf Libyan Bank), but the amount is immaterial and may indeed be a benefit in the event of post-war rebuilding.

Little in the way of private sector growth yet

As have other banks in the UAE, FGB has seen little growth in 1Q11, with loans rising just 1.7% qoq. Indeed, FGB isn't overly optimistic either about private sector lending going forward. Similarly to its competitors, it sees most growth in the sovereign sector, driven by generally large-ticket projects in energy, manufacturing and infrastructure. Nevertheless, an acceleration to double-digit levels remains elusive.

Valuation trades at a small premium to the sector

FGB trades at a P/B of 1.05x 2012F (making it the most expensive in the sector bar National Bank of Abu Dhabi), after rising back towards the top of its established trading range. We believe this is justified by the lower country risk profile, but with operating earnings momentum likely to be in negative territory this coming quarter, we reduce our recommendation to Hold (from Buy). We raise our DDM-based target price to Dh19.99 (from Dh18.78) due mostly to a reduction in the discount rate and roll forward of our pricing date.

Important disclosures can be found in the Disclosures Appendix.

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Income statement

| Dhm | FY09A | FY10A | FY11F | FY12F | FY13F |
|----------------------------------|-------------|-------------|-------------|-------------|-------------|
| Net interest income | 3834 | 4257 | 4760 | 5085 | 5780 |
| Non-interest income | 2295 | 2086 | 1650 | 1813 | 2159 |
| Total income | 6129 | 6343 | 6410 | 6898 | 7939 |
| Operating costs | -1147 | -1170 | -1220 | -1328 | -1688 |
| Goodwill (amort/impaird) | n/a | n/a | n/a | n/a | n/a |
| Other costs | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| <u>Pre-prov operating profit</u> | 4982 | 5173 | 5190 | 5570 | 6251 |
| Provisions charges | -1680 | -1639 | -1484 | -746.9 | -561.9 |
| <u>Post-prov op prof</u> | 3301 | 3534 | 3706 | 4823 | 5689 |
| Associates (pre-tax) | 29.0 | -37.8 | 28.8 | 39.8 | 42.6 |
| Other pre-tax items | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Reported PTP | 3331 | 3496 | 3735 | 4863 | 5732 |
| Taxation | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Minority interests | -2.63 | -123.9 | -9.87 | -9.87 | -9.87 |
| Preference dividends | -120.0 | -240.0 | -240.0 | -240.0 | -240.0 |
| Other post-tax items | 102.4 | 288.0 | 290.4 | 292.2 | 300.1 |
| Reported net profit | 3310 | 3420 | 3776 | 4905 | 5782 |
| Tot normalised items | -83.6 | 0.00 | 0.00 | 0.00 | 0.00 |
| Normalised PTP | 3331 | 3496 | 3735 | 4863 | 5732 |
| Normalised net profit | 3394 | 3420 | 3776 | 4905 | 5782 |

Source: Company data, Rasmala forecasts

year to Dec

Balance sheet

| Dhm | FY09A | FY10A | FY11F | FY12F | FY13F |
|-----------------------------------|---------------|---------------|---------------|---------------|---------------|
| Net loans to customers | 90386 | 95628 | 102249 | 114003 | 127921 |
| Other int earn assets | 18199 | 25079 | 27358 | 31026 | 36679 |
| Goodwill | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Oth non-int earn assets | 5340 | 4475 | 7825 | 9777 | 10064 |
| Total assets | 125473 | 140758 | 151338 | 168751 | 188860 |
| Total customer deposits | 86422 | 98742 | 105578 | 117715 | 132086 |
| Oth int-bearing liabs | 11761 | 13251 | 14158 | 14879 | 15167 |
| Non int-bearing liab | 5064 | 5034 | 4987 | 5561 | 9708 |
| Total liabilities | 103247 | 117027 | 124723 | 138156 | 156961 |
| Share capital | 17841 | 19226 | 22110 | 26090 | 27395 |
| Reserves | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Total equity (excl min) | 21841 | 23226 | 26110 | 30090 | 31395 |
| Minority interests | 384.9 | 504.8 | 504.8 | 504.8 | 504.8 |
| Total liab & sh equity | 125473 | 140758 | 151338 | 168751 | 188860 |
| Risk weighted assets | 123911 | 127351 | 136168 | 151822 | 170357 |
| Est non-perf loans | n/a | n/a | n/a | n/a | n/a |
| Specific provisions | -2530 | -3295 | -4449 | -4751 | -4838 |
| General provisions | n/a | n/a | n/a | n/a | n/a |

Source: Company data, Rasmala forecasts

year ended Dec

Capital

| Dhm | FY09A | FY10A | FY11F | FY12F | FY13F |
|---------------------------|--------|--------|--------|--------|--------|
| Risk weighted assets | 123911 | 127351 | 136168 | 151822 | 170357 |
| Reported net profit | 3310 | 3420 | 3776 | 4905 | 5782 |
| Opening risk assets | 110350 | 123911 | 127351 | 136168 | 151822 |
| Closing risk assets | 123911 | 127351 | 136168 | 151822 | 170357 |
| Change in risk assets | 13561 | 3441 | 8817 | 15653 | 18535 |
| Capital required | 1356 | 344.1 | 881.7 | 1565 | 1853 |
| Free capital flow | 2074 | 3316 | 3134 | 3580 | 4169 |
| Ordinary dividend paid | -677.0 | -900.0 | -566.9 | -632.8 | -4177 |
| Share buy back/spec div | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Equity / preference issue | -154.0 | -857.5 | 0.00 | 0.00 | 0.00 |
| Cash flow from financing | -831.0 | -1757 | -566.9 | -632.8 | -4177 |
| Net capital flow | 1243 | 1559 | 2567 | 2947 | -8.91 |
| Tier 1 capital | 22930 | 24532 | 27536 | 31681 | 33040 |
| Tier 1 capital ratio (%) | 18.5 | 19.3 | 20.2 | 20.9 | 19.4 |

Source: Company data, Rasmala forecasts

year to Dec

Standard ratios

| | First Gulf Bank | | | | | Ntl Bank of Abu Dhabi | | | Emirates NBD | | |
|---------------------------|-----------------|-------|-------|-------------|-------|--------------------------|-------------|-------|--------------|-------------|-------|
| | FY09A | FY10A | FY11F | FY12F | FY13F | FY11F | FY12F | FY13F | FY11F | FY12F | FY13F |
| Performance | | | | | | | | | | | |
| Non-int inc/gr op inc (%) | 37.4 | 32.9 | 25.7 | 26.3 | 27.2 | 26.4 | 27.7 | 27.4 | 27.4 | 28.7 | 29.5 |
| Cost/income (%) | 18.7 | 18.4 | 19.0 | 19.3 | 21.3 | 30.9 | 32.0 | 32.8 | 35.4 | 33.1 | 32.5 |
| Costs/average assets (%) | 0.98 | 0.88 | 0.84 | 0.83 | 0.94 | 1.10 | 1.15 | 1.20 | 1.20 | 1.16 | 1.14 |
| Net income growth (%) | 10.5 | 7.68 | 6.83 | 30.2 | 17.9 | 2.31 | 24.6 | 22.0 | 78.6 | 32.7 | 19.0 |
| Net cust loan growth (%) | 13.9 | 5.80 | 6.92 | 11.5 | 12.2 | 9.20 | 15.0 | 15.2 | 2.29 | 8.89 | 10.6 |
| Cust deposit growth (%) | 16.8 | 14.3 | 6.92 | 11.5 | 12.2 | 9.22 | 15.0 | 15.2 | 4.85 | 8.89 | 10.6 |
| Net interest margin (%) | 3.76 | 3.62 | 3.69 | 3.58 | 3.62 | 2.91 | 2.84 | 2.86 | 2.88 | 2.89 | 2.86 |
| Return on avg assets (%) | 3.02 | 2.84 | 2.76 | 3.22 | 3.37 | 1.86 | 2.10 | 2.26 | 0.90 | 1.90 | 2.05 |
| Return on avg equity (%) | 20.2 | 18.5 | 18.3 | 20.4 | 21.6 | 18.2 | 19.7 | 21.4 | 7.68 | 16.7 | 18.1 |
| RORWA (%) | 2.90 | 2.72 | 2.87 | 3.41 | 3.59 | 2.37 | 2.64 | 2.79 | 1.05 | 2.38 | 2.57 |
| | | | | year to Dec | | | year to Dec | | | year to Dec | |
| Valuation | | | | | | | | | | | |
| Normalised EPS growth (%) | 3.29 | -3.52 | 14.0 | 35.6 | 18.8 | 0.23 | 26.3 | 23.2 | -0.55 | 155.7 | 20.0 |
| Reported PE (x) | 9.09 | 9.18 | 8.05 | 5.93 | 4.99 | 9.21 | 7.29 | 5.92 | 5.86 | 4.35 | 3.62 |
| Normalised PE (x) | 8.85 | 9.18 | 8.05 | 5.93 | 4.99 | 9.21 | 7.29 | 5.92 | 11.1 | 4.35 | 3.62 |
| Price/book value (x) | 1.61 | 1.50 | 1.24 | 1.05 | 1.00 | 1.46 | 1.27 | 1.16 | 0.72 | 0.66 | 0.60 |
| Price/adjusted BVPS (x) | n/a | n/a | n/a | n/a | n/a | n/a | n/a | n/a | n/a | n/a | n/a |
| Dividend yield (%) | 2.70 | 3.29 | 2.07 | 2.31 | 15.3 | 1.96 | 3.48 | 9.04 | 4.52 | 9.19 | 12.4 |
| | | | | year to Dec | | | year to Dec | | | year to Dec | |
| Per share data | FY09A | FY10A | FY11F | FY12F | FY13F | Solvency | FY09A | FY10A | FY11F | FY12F | FY13F |
| Tot adj dil sh, ave (m) | 1556 | 1575 | 1538 | 1500 | 1500 | Tier 1 capital ratio (%) | 18.5 | 19.3 | 20.2 | 20.9 | 19.4 |
| Pre-prov prof/share (AED) | 3.20 | 3.28 | 3.38 | 3.71 | 4.17 | Total CAR (%) | 22.3 | 23.0 | 24.2 | 24.9 | 23.2 |
| Reported EPS (AED) | 2.01 | 1.99 | 2.27 | 3.08 | 3.65 | Equity/assets (%) | 17.4 | 16.5 | 17.3 | 17.8 | 16.6 |
| Normalised EPS (AED) | 2.06 | 1.99 | 2.27 | 3.08 | 3.65 | Net cust loans/dep (%) | 104.6 | 96.8 | 96.8 | 96.8 | 96.8 |
| Book value per sh (AED) | 11.3 | 12.2 | 14.7 | 17.4 | 18.3 | Rep NPL/gr cus adv (%) | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Dividend per share (AED) | 0.49 | 0.60 | 0.38 | 0.42 | 2.78 | Tot prov/rep NPLs (%) | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Dividend cover (x) | 5.01 | 3.80 | 6.66 | 7.75 | 1.38 | Bad debts/advances (%) | 1.81 | 1.66 | 1.39 | 0.63 | 0.42 |
| | | | | year to Dec | | | | | | year to Dec | |

Priced as follows: FGB.AD - Dh18.25; NDAB.AD - Dh11.30; ENDB.DU - Dh4.09
Source: Company data, Rasmala forecasts

Valuation methodology

| Stage 1 (2010-2013) | | 4q10 | 4q11 | 2012 | 2013 |
|--------------------------|-----------------------------|----------------------|--------|---------------|---------------|
| Explicit Dividends | Forecast CF to shareholders | 1,288 | 567 | 633 | 4,177 |
| NPV Stage 1 | 4,317 | 5,065 | 4,317 | 4,287 | 4,177 |
| Stage 2 (2014-23) | | Model Numbers | | | |
| Modelled Dividends | Excess Capital | ROE1 | Growth | Capital Req'd | RWA |
| | Modelled Dividends | 23% | 15% | 15,332 | 170,357 |
| NPV Stage 2 | 16,672 | | | | |
| Stage 3 (2024+) | | Model Numbers | | | |
| Terminal Value | 2023 | ROE1 | Growth | Capital Req'd | |
| | | 12% | 6% | 62,027 | |
| NPV Stage 3 | 8,997 | | | | |
| Total NPV | | COE | | | |
| Stage 1 (2010-2013) | 4,317 | US RFR | | | 3.31% |
| Stage 2 (2014-23) | 16,672 | Country Risk Spread | | | 5.00% |
| Stage 3 (2024+) | 8,997 | Sector Risk Spread | | | 3.00% |
| NPV | 29,987 | Stock Spread | | | 3.00% |
| Shares | 1,500 | Discount Rate | | | 14.31% |
| Price Target | 19.99 | | | | |
| Price | 18.25 | | | | |
| Upside/(Downside) | 10% | | | | |

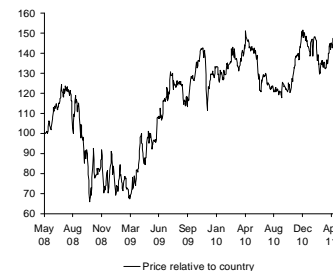
Source: Rasmala forecasts

Company description

Hold

Price relative to country

First Gulf Bank, headquartered in Abu Dhabi, was established in 1979 and provides financial services in various businesses through a network of 19 branches across the Emirates. FGB remains one of the best-performing local banks, as its operating income and net profit delivered CAGRs of 78% and 70%, respectively, during 2002-09. As of March 2010, the bank's market share in loans and deposits amounted to 9.1% and 8.8%, respectively, representing increases of 72bp and 114 bp over a year. FGB is 66.9% owned by the members of the Abu Dhabi Ruling Family, and has a freefloat of 26.4%.



Strategic analysis

Average SWOT company score:

2

Loan split, 2010

Strengths

Highest NIMs with the lowest cost-income ratio provide it with comparatively high ROEs. A low LD ratio also provides FGB the capability to win market share in the UAE.

Weaknesses

High exposure to retail loans and significant property exposure (worth 62% of common equity) remain the top weaknesses of FGB.

Opportunities

The primary opportunities for FGB are increasing its international branch network (and thus achieving geographical diversification) and its capability to increase leverage to fuel growth.

Threats

Significant decline in oil prices (thus limiting country growth rates) or geo-political instability remain top threats for UAE banks.

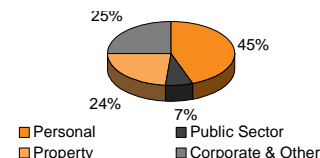
Scoring range is 1-5 (high score is good)

3

1

2

2



Source: Company reports

Market data

Headquarters

First Gulf Bank Building, Al Khalidiya Street, P.O. Box 6316, Abu Dhabi, UAE

Website

www.fgb.ae

Shares in issue

1500.0m

Freefloat

26%

Majority shareholders

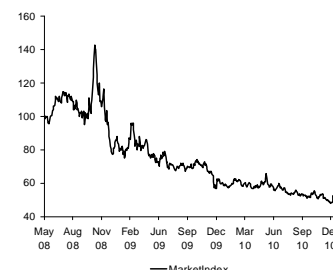
Abu Dhabi Ruling Family Members (61%), Direct Access Investments (7%)

Country view: United Arab Emirates

Country rel to M East & Africa

MENA markets are showing characteristics of a text book case of loss aversion. This is expected given the magnitude of losses investors experienced since 2008, with 2009 lagging emerging markets by a fairly wide margin. Rising oil prices and budget surpluses drove asset prices across the region higher resulting in a real-estate bubble that has negatively impacted speculators and the banking system. Bubbles do pop and recover over time if there is a legal system in place that enables the transfer of assets. The bad news is such a mechanism did not exist. The good news is that with the creation or RERA and the possibility of Strata Law, this could change and facilitate the transfer of properties from speculators to real investors.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score:

4+

Broker recommendations

Supplier power

The lack of significant regulator control allows the banks to change contract arrangements (such as the base rate). This substantially increases the supplier power for all banks in the UAE.

Barriers to entry

Strong local government ownership in most banks coupled with branch limits for foreign banks keeps barriers to entry high for this sector.

Customer power

Customer power is extremely low in the UAE, as any change in bank policies has to be accepted by clients. Points of contact at institutions remain limited, thus raising customer redressal issues.

Substitute products

We believe the availability of substitute products (capital markets and syndicate loans) has diminished in recent times, thus improving margin capabilities for banks in the core interest business.

Rivalry

Competition (and price war) among local banks is low. However, recent low growth has forced a few newer institutions to lower product prices, indicating a trend towards more competition long term.

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse

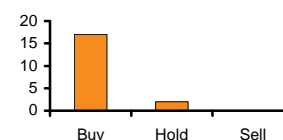
3+

4+

5+

4+

4+



Source: Bloomberg

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Valuation and risks to target price

First Gulf Bank (RIC: FGB.AD, Rec: Hold, CP: Dh18.25, TP: Dh19.99): We base our valuation on a 3-stage DDM: a 3-year stage of explicit forecasts, a 10-year stage of trend forecasts and a terminal stage based on a GGM. The primary downside risk to our GGM-derived valuation and target price is regulatory risk, property market deterioration and increasing competition. On the positive side, a return to private sector corporate growth should benefit FGB, while stabilisation of the Maghreb may also provide a longer-term opportunity.

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