Dubai Financial Market (DFM)

FY08 Update

Target Price	Market Price	Recommendation	Upside Potential	Investment Grade
AED1.42	AED1.39	Hold	2.2%	Speculative

Share Data

Report Date	**April 13, 2009**
Company Abbreviation	DFM
Sector	Financials
Traded Market	DFM
Report Reason	FY08 Update
Valuation Methodology	DCF
Previous Report Date	October 28, 2008
Previous Target	AED3.97
Exchange Rate	AED3.67/USD1
Stock Currency	AED
Reuters Code	DFM.DU
Outstanding Shares (mln)	8,000
Par Value/Share (AED)	AED1
Financial Year Ending	December
Mkt. Cap (AED mln)	11,600
Weight to (PEMI)	4.81%
Price Low – High (AED) (52Wk.)	0.76 — 6.2
Relative Performance (52Wk.)	-4.9%

Shareholders	Ownership Stake
Dubai Gov. — Borse Dubai	80%
Free Float	20%

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Trading revenue dropped 19.1% y-o-y in FY08 to AED640 million as trading value slid 19.5% y-o-y to AED305 billion, buoyed by strong performance in 1Q08 (AED125 billion). Total trading values in 2Q08 and 3Q08 were each around half of 1Q08 turnover at AED78 billion and AED64 billion, respectively, as Average Daily Turnover (ADT) echoed the drop, but turnover in 4Q08 was significantly lower registering only AED38 billion (ADT of AED672 million, 67% below 1Q08 and 33% below 3Q08).

DFM managed to shrink its expenses by 12.9% y-o-y as total revenue dropped by 16.7% in FY08, cutting staff bonuses by 87% from AED16 million in FY07 to AED2 million. The company recorded net investment revenue of AED263 million for FY08, 121% higher than in FY07 on the back of AED105 million in returns on Islamic investment deposits and AED130 million as gains from the sale of AFS investments.

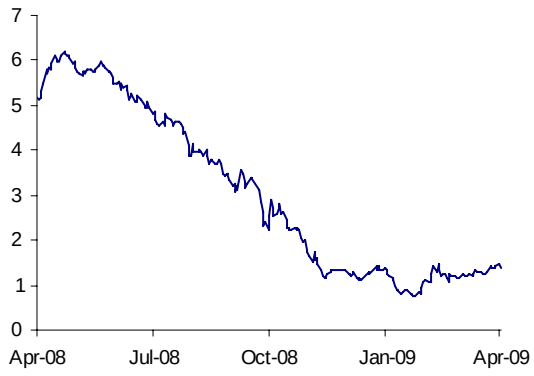
The company announced that it will pay out 105% of FY08 profits as dividends (8% cash dividend versus 10% in FY07) in a move to assist Borse Dubai in its debt repayment. In the annual general meeting, the company's shareholders also ratified the board of directors' suggestion to discontinue the 10% annual deduction allocated to the general reserve account.

Dubai Financial Market's planned new headquarters in Business Bay, a development costing ca. AED1 billion, has been placed on hold after the company realized an investment revaluation loss of AED1.27 billion in 2H08, which was accounted for directly under shareholders' equity.

Our base case assumptions for DFM's future trading activity assumes a 50% y-o-y drop in ADT in FY09 to AED620 million versus AED1,240 million in FY08, which reflects into AED310 million of trading revenue for FY09 (AED361 total revenue, 48% drop y-o-y). Our ADT for FY09 is 37% higher than that achieved in 1Q09 (AED452 million) since we expect a slight increase in the second half as global markets recover. Our optimistic scenario assumes a better recovery in ADT this year to AED992 million versus AED452 million in 1Q09 and record ADT of AED1,786 million in FY10 as the market recovers from the recent crash with more money being attracted to the UAE due to its strong macroeconomic fundamentals.

Our revised valuation for the base case scenario of DFM has yielded a DCF value of AED1.42/share, down 64.2% from our previous target price of AED3.97/share, and 2.2% above the current market price of AED1.39. We accordingly issue a hold recommendation on this stock.

Stock Performance Chart
(AED / Share)



Fiscal Year	2007a	2008a	2009f	2010f	2011f
Revenues	827	689	361	612	782
Growth	4.8%	-16.7%	-47.6%	69.4%	27.8%
EBITDA Margin	90.4%	89.9%	80.3%	87.2%	88.9%
Net Income	1,440	605	306	573	758
EPS (AED)	0.18	0.08	0.04	0.07	0.09
EPS Growth	80.5%	-58.0%	-49.4%	87.3%	32.4%
DPS (AED)	0.10	0.08	0.02	0.05	0.07
Book Value / Share (AED)	1.10	0.95	1.00	1.08	1.13
P/E (x)	7.72	18.38	36.36	19.42	14.67
Dividend Yield	7.1%	5.7%	1.4%	3.9%	5.1%
P/BV (x)	1.26	1.46	1.40	1.29	1.24

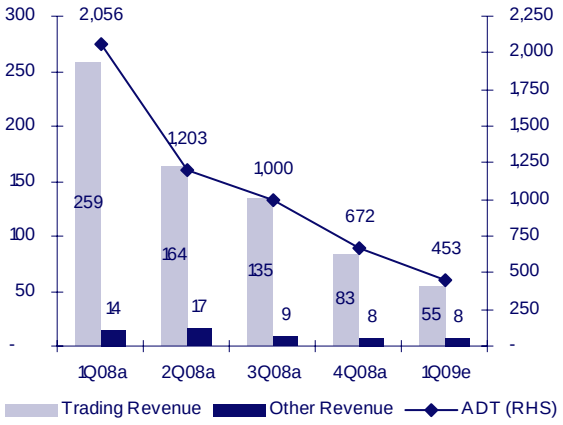
Please refer to disclaimer on last page

Figures are in AED mln unless stated otherwise Source: Company Historical & Prime Estimates

Trading Revenue Fell 19.1% y-o-y in FY08 along with Turnover as Stock Prices Crashed and Investor Appetite Shifted to Safer Assets

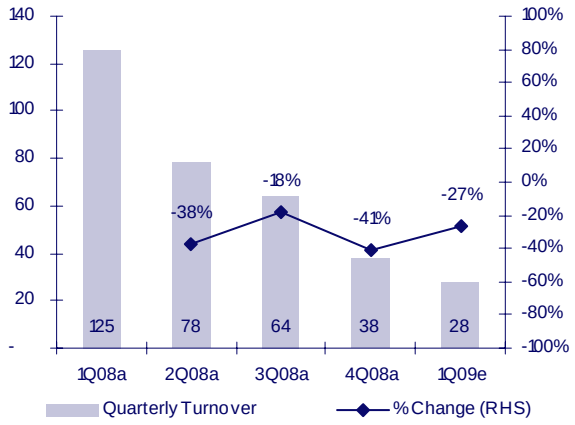
The recent market crash was characterized by an outflow of foreign funds combined with low trading volumes as bank lending was drastically reduced and investors sought safer assets like bonds, sukuks and cash, which resulted in low demand for stocks and a steep drop in prices. Trading revenue dropped 19.1% y-o-y in FY08 to AED640 million as trading value slid 19.5% y-o-y to AED305 billion, buoyed by strong performance in 1Q08 (AED125 billion). Total trading values in 2Q08 and 3Q08 were each around half of 1Q08 turnover at AED78 billion and AED64 billion, respectively, as Average Daily Turnover (ADT) echoed the drop, but turnover in 4Q08 was significantly lower registering only AED38 billion (ADT of AED672 million, 67% below 1Q08 and 33% below 3Q08).

Figure 1: **Quarterly Revenue & ADT** (AED mln)



Source: DFM, Prime estimates

Figure 2: **Quarterly Turnover** (AED bln)



Source: DFM, Prime estimates

General and Administrative Expenses Drop as Staff Bonus is Cut

The DFM managed to shrink its expenses by 12.9% y-o-y as total revenue dropped by 16.7% in FY08, cutting staff bonuses by 87% from AED16 million in FY07 to AED2 million. Professional expenses also dropped by 73% to AED2 million but payrolls expanded by 23% to AED44 million as the company prepared for expansion in early FY08 (no layoffs were reported). The DFM recorded net investment revenue of AED263 million for FY08, 121% higher than in FY07 on the back of AED105 million in returns on Islamic investment deposits and AED130 million as gains from the sale of AFS investments.

Dividend Payout of 105% for FY08 to support Borse Dubai's Debt Repayment and a Discontinuation of the 10% Annual General Reserve Transfer

DFM's parent company, government-owned Borse Dubai with an 80% stake in DFM, has been struggling to refinance its USD3.8 billion worth of debt maturing in FY09, which was used to finance its investment into the NASDAQ OMX Group earlier. However, Borse Dubai managed to secure a Term Loan Facility worth USD2.5 billion in February 2009 for the purpose of refinancing this debt, with the balance to be generated internally. The DFM announced that it will pay out 105% of FY08 profits as dividends (8% cash dividend versus 10% in FY07) in a move to assist Borse Dubai in its debt repayment. In the annual general meeting, the company's shareholders also ratified the board of directors' suggestion to discontinue the 10% annual deduction allocated to the general reserve account, keeping the other 10% annual transfer to each of the special and statutory reserves intact.

Construction of Business Bay Premises Postponed Until Further Notice after AED1.27 billion Investment Revaluation Loss in FY08

Dubai Financial Market's planned new headquarters in Business Bay, a development costing ca. AED1 billion, has been placed on hold after the company realized an investment revaluation loss of AED1.27 billion in 2H08, which was accounted for directly under shareholders' equity. According to the company, the new premises that was expected to generate significant rental income to the DFM has been postponed for at least one year, and possibly more, in light of heavy investment losses and a large drop in trading activity on the exchange, where ADT in 1Q09 fell 78% y-o-y to only AED453 million (33% drop q-o-q).

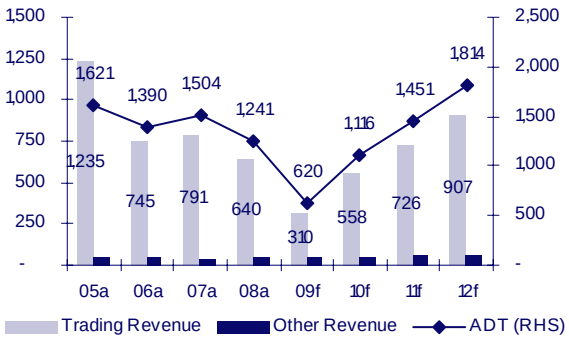
Base Case Indicates a Target Price of AED1.42, 2.2% Above Market

Business worsened further in 1Q09 as turnover slumped another 27% q-o-q to register AED28 billion (78% y-o-y drop) with the company expected to have generated only AED55 million in trading revenues during this period (ADT of 453 million). However, February and March 2009 witnessed a few days of strong trading activity with turnover rising above the AED1 billion mark suggesting that a recovery from the period of ultra-low turnover may be in sight.

Our base case assumptions for DFM's future trading activity assumes a 50% y-o-y drop in ADT in FY09 to AED620 million versus AED1,240 million in FY08, which reflects into AED310 million of trading revenue for FY09 (AED361 total revenue, 48% drop y-o-y). Our ADT for FY09 is 37% higher than that achieved in 1Q09 (AED452 million) since we expect a slight increase in the second half as global markets recover. The base case also assumes that ADT in FY10 will reach AED1,116 million, approaching the AED1,241 million achieved in FY08 as a return of investors and speculators to the market indicates a recovery in trading volumes.

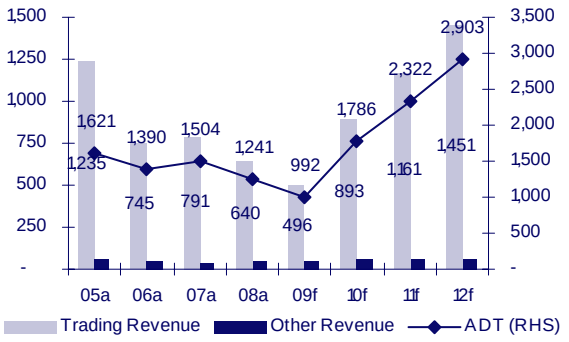
This scenario assumes a very slight increase in the company's expenses during FY09 with the number rising only 3% as the company keeps a tight grip on spending while trading activity remains sluggish. We have also assumed average returns of 8% per annum on the company's Islamic Investment deposits going forward, and accounted for steady upside revaluations of AFS investments directly in the investment reserves account. These base case assumptions imply an adjusted DCF price target of AED1.42/share for DFM, which is 2.2% above the current market price.

Figure 3: **Base Case — Revenue & ADT** (AED mln)



Source: DFM, Prime estimates

Figure 4: **Bullish — Revenue & ADT** (AED mln)



Source: DFM, Prime estimates

Bullish Scenario Assumes Higher Turnover and a Higher Upward Revaluation of AFS Investments; Investment Income is Unchanged from Base Case Due to Low Visibility

Our bullish scenario assumes a better recovery in ADT this year to AED992 million versus AED452 million in 1Q09 and record ADT of AED1,786 million in FY10 as the market recovers from the recent crash with more money being attracted to the UAE due to its strong macroeconomic fundamentals. This would reflect into a y-o-y drop of 22% in trading revenue in FY09 (versus 52% drop in the base case) with expenses rising in parallel to AED79 million (16% of revenue) and a DCF price target of AED2.13/share.

Turnover would continue at CAGR 27% between FY11-FY13 as the market continues to evolve and the company would experience a higher upward revaluation of its AFS investments in this bullish case, but such revaluations will not directly affect cash flows since we do not assume gains from sales of AFS assets in our forecasts. We also kept our forecasts of returns on Islamic investment deposits constant at 8% in these optimistic scenarios due to low visibility.

It is worth noting that DFM's stock price movement is highly correlated with that of the DFM General Index, which may potentially lead the price to deviate (to the upside) from the fundamentals described here in the case of a short-term bear market correction (upward rally).

DCF Price Target

Our revised valuation for the base case scenario of DFM has yielded a DCF value of AED1.42/share, down 64.2% from our previous target price of AED3.97/share, and 2.2% above the current market price of AED1.39. We accordingly issue a hold recommendation on this stock.

Table 1: **DFM Turnover Scenarios and Price Targets** (AED mln)

		2008a	2009f	2010f	2011f	2012f
Base Case Scenario						
Trading Revenue		640	310	558	726	907
Average Daily Turnover		1,241	620	1,116	1,451	1,814
Target Price	**1.42**					
Bullish Scenario						
Trading Revenue		640	496	893	1,161	1,451
Average Daily Turnover		1,241	992	1,786	2,322	2,903
Target Price	**2.13**					

Source: DFM, Prime Estimates

FINANCIAL SUMMARY
(Figures in AED million)

Income Statement	2007a	2008a	2009f	2010f	2011f
Revenues	**827.3**	**688.9**	**361.2**	**611.9**	**782.1**
Growth	*4.8%*	*-16.7%*	*-47.6%*	*69.4%*	*27.8%*
S,G & Admin. Expenses	79.8	69.4	71.3	78.2	87.1
EBITDA	**747.5**	**619.4**	**289.9**	**533.7**	**695.0**
Growth	*1.8%*	*-17.1%*	*-53.2%*	*84.1%*	*30.2%*
EBITDA Margin	90.4%	89.9%	80.3%	87.2%	88.9%
Depreciation & Amortization	85.6	88.7	88.8	87.0	87.5
Other Provisions	0.0	250.0	0.0	0.0	0.0
Operating EBIT	**661.9**	**280.7**	**201.1**	**446.8**	**607.5**
Interest Income	0.0	0.0	0.9	1.4	1.2
Investment Income	119.2	263.2	103.8	124.5	149.4
Non-Operating Revenues	468.0	0.0	0.0	0.0	0.0
Pre Tax Income	**1,249.2**	**543.9**	**305.8**	**572.7**	**758.2**
Pre Tax Income Growth	*57%*	*-56%*	*-44%*	*87%*	*32%*
NPAT	**1,249.2**	**543.9**	**305.8**	**572.7**	**758.2**
Growth	*56.6%*	*-56.5%*	*-43.8%*	*87.3%*	*32.4%*
Extraordinary Items	190.4	61.0	0.0	0.0	0.0
Net Income	**1,439.6**	**605.0**	**305.8**	**572.7**	**758.2**
Growth	*80.5%*	*-58.0%*	*-49.4%*	*87.3%*	*32.4%*
ROS	174.0%	87.8%	84.7%	93.6%	96.9%

Balance Sheet	2007a	2008a	2009f	2010f	2011f
Cash & Marketable Securities	2,803.7	1,667.6	1,398.6	1,743.9	1,942.0
Trade Receivables-Net	56.2	33.6	25.3	42.8	54.7
Other Current Asset	1.1	4.6	4.8	5.0	5.3
Total Current Asset	**2,861.0**	**1,705.8**	**1,428.7**	**1,791.8**	**2,002.0**
Net Fixed Assets	312.7	308.4	314.3	322.1	333.7
Other Assets	7,049.4	6,622.2	6,746.3	7,320.5	7,644.6
Total Assets	**10,223.2**	**8,636.4**	**8,489.3**	**9,434.4**	**9,980.4**
Accounts Payable	288.8	54.3	36.1	61.2	78.2
Dividend Payable	794.6	635.0	152.9	429.5	568.6
Other Current Liabilities	48.5	48.5	48.5	48.5	48.5
Total Current Liabilities	**1,131.9**	**737.8**	**237.5**	**539.2**	**695.3**
Provisions for Deferred Income	280.0	280.0	280.0	280.0	280.0
Provisions	2.0	2.6	2.8	3.1	3.4
Total Shareholders' Equity	**8,809.3**	**7,616.0**	**7,968.9**	**8,612.1**	**9,001.6**
Total Liabilities & Shareholders' Equity	**10,223.2**	**8,636.4**	**8,489.3**	**9,434.4**	**9,980.4**

Free Cash Flow Statement	2007a	2008a	2009f	2010f	2011f
NOPLAT	**661.9**	**280.7**	**201.1**	**446.8**	**607.5**
Non-Cash Items	85.6	338.7	88.8	87.0	87.5
Gross Cash Flow	**747.5**	**619.4**	**289.9**	**533.7**	**695.0**
Gross Investments	113.4	-133.4	22.9	164.2	220.1
Operating Cash Flow	634.1	752.8	267.0	369.6	474.9
Non-Operating Cash Flow	658.4	61.0	0.0	0.0	0.0
Free Cash Flow Ex Intangibles	**1,292.6**	**813.9**	**267.0**	**369.6**	**474.9**
Free Cash Flow Before Financing	**-4,537.0**	**813.9**	**267.0**	**369.6**	**474.9**
Financing Flow:					
Interest Income After-Tax	0.0	0.0	-0.9	-1.4	-1.2
Investment Income After-Tax	-119.2	-263.2	-103.8	-124.5	-149.4
Increase in Excess Cash & M. Sec.	1,576.9	-1,130.2	-263.1	342.8	196.4
Change in Subsidiaries & Long Term Investments	0.0	0.0	0.0	0.0	0.0
After-Tax Interest Expense	0.0	0.0	0.0	0.0	0.0
Decrease in Debt & Bonds	0.0	0.0	0.0	0.0	0.0
Provisions Used	-0.8	249.4	-0.3	-0.3	-0.3
Dividends Paid	0.0	794.6	635.0	152.9	429.5
Non-Appropriation Items	0.0	0.0	0.0	0.0	0.0
Shareholders Equity	-5,993.8	1,163.3	0.0	0.0	0.0
Total Financing Flow	**-4,537.0**	**813.9**	**267.0**	**369.6**	**474.9**

Source: Company Financials, Prime Projections

Stock Recommendation Guidelines	
Recommendation	**Target-to-Market Price (x)**
Strong Buy	x > 25%
Buy	15% < x <25%
Accumulate	5%< x <15%
Hold	-5% < x < 5%
Reduce	-15% < x < -5%
Sell	-25% < x < -15%
Strong Sell	x < -25%

Investment Grade	Explanation
Growth	3 Yr. Earnings CAGR > 20%
Value	Equity Positioned Within Maturity Stage of Cycle
Income	Upcoming Dividend Yield > Average LCY IBOR
Speculative	Quality Earnings Reflect Above Normal Risk Factor

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