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Subject: Elaboration on Credit Rating

Gulf Finance House (GFH) would like to share further details with its shareholders on the recent credit rating assigned by Capital Intelligence (CI).

Capital Intelligence (CI) in its announcement declared the following; while assigning GFH with Long and Short-Term Ratings of 'BB-' and 'B', respectively.

"The ratings were supported by a significant reduction in leverage as a result of debt repayment and increases in equity, the successful restructuring of debt with an extended repayment period, and the return to profitability in 2012. The factors currently constraining the ratings were the forced debt restructuring in 2012, tight liquidity (although this improved in H1 2013), an encumbered asset base, a small balance sheet coupled with single name and sector concentrations in the asset base, reliance on deal flow for income generation, and the still challenging investment environment.

In view of the improvement in both liquidity and leverage in H1 2013, a 'Positive' Outlook is assigned to the ratings. To achieve an improvement in the rating would require GFH to be able to demonstrate successful repayment of restructured debt, further improvement in liquidity and financial flexibility, as well as sustained strong profitability and cash flow. Concurrently GFH would also need to maintain the improving leverage trend.

GFH, in common with other Islamic and conventional investment companies in the Gulf Cooperation Council (GCC) region, had suffered a major setback in credit metrics and operations following the domestic and regional financial crisis in 2009. As well as experiencing a dramatic worsening of asset quality, the company was also hit by a severe liquidity squeeze which forced debt restructuring and suspension of new investment. GFH has since that time successfully paid down debt and restructured term financings with lenders. Concurrently leverage has improved noticeably due to the twin effect of debt repayment and increases in equity (under the convertible murabaha programme) over the past two years.

GFH's sources of funding are currently adequate, but its liquidity is rather tight notwithstanding the improvement in ratios in H1 2013. The low liquidity reflects the modest holdings of cash and bank balances. GFH's financial flexibility is projected to remain limited due to the large proportion of assets pledged as security to lenders. That said, the shares in associate 'Khaleeji Commercial Bank' (an Islamic retail bank in Bahrain) are quoted and could provide a possible source of cash liquidity in the event GFH opted to sell a part of its significant stake.

Although total income slipped in 2012, both net profit and ROAA recovered due to a significant decline in operating costs. GFH's returns are still modest however and underscore limited recurring revenue streams and reliance on deal flow for income generation. Management's projections for the near term envisage a sustained recovery in profitability boosted by income from investment advisory services, which are viewed by CI as being of higher quality, and direct investments. While the improved cash flow will aid liquidity it is more than likely that GFH's debt servicing will remain reliant on asset sales to some extent, although this is partly inherent in the company's business model as an investment company".

- **Long-term Rating:**

***BB**, a Speculative Grade,* refers to speculative credit quality. Capacity for timely fulfillment of financial obligations is vulnerable to adverse changes in internal or external circumstances. Financial and/or non-financial factors do not provide significant safeguard and the possibility of investment risk may develop.

- **Short-term Rating:**

***B**, a Speculative Grade,* refers to an adequate capacity for timely repayment that could be seriously affected by unexpected adversities.

Note: The (-) or the (+) is added to the rating based on the discretion of the rating agency. This symbolizes the *weightage* of the rating granted.

Management opinion on the assigned Credit Rating:

"The Management believes that the recent rating is an endorsement of the actions taken by the Bank and its shareholders to strengthen the Bank's financial position. The rating will strengthen market confidence in the Bank and allow for better business opportunities in the future".

The bank's rating based on the financial results of Q1-2013; it is important to note that the Bank has further significantly bolstered its liquidity position which is reflected in the financial results of Q2-2013.

Yours Sincerely,

Nabeel Mirza
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