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Banks - Forecast of 2018 Q4 Results

Banks, Poland

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The fourth quarter of 2018 is shaping up to be a record one for the Polish bank sector, with the aggregate net income generated by covered institutions expected to show a 13.9% rebound from the previous quarter after growing 5.2% year over year. The stellar 2018 financials set the scene for potentially bumper profits in the year ahead, indicating sizable upside potential as bank stocks continue to trade at low multiples.

It is important to note that the strong figures anticipated in Q4 2018 were driven first and foremost by core business activities, reflected in 3.6% likely quarter-on-quarter expansion in aggregate net interest income and a 2.5% increase in fee income generated amid a challenging environment in capital markets. Adding to the bullish factors were expanding net interest margins, with aggregate NIM showing a continued rise of 3bp, coupled with strong consumer loan origination volumes even after slight contraction from the previous quarter.

The strong underlying recurring Q4 results will be impacted by a variety of one-time factors, including a "bad-will" gain on the one hand, and merger-related costs on the other hand, anticipated at Santander Bank Polska, with some banks likely to have written off parts of their corporate loan receivables, and others generating one-time gains from securities trades and NPL sales.

Summing up, a robust fourth-quarter earnings season should improve sentiment for the Polish bank sector, and reinforce analysts in their current expectations for FY2019 after a string of revisions.

Summary of 2014 Q4 net income estimates

(PLN m)	mDM	Q/Q	Y/Y	consensus	differ. (%)
PKO BP	1,001	-4%	22%	956	4.7%
Pekao	673	-10%	-44%	679	-0.9%
Santander	869	75%	58%	930	-6.6%
ING	404	7%	10%	420	-3.8%
Millennium	185	-8%	3%	198	-6.8%
Handlowy	172	8%	5%	165	4.0%
Alior Bank	176	2%	1%	203	-13.0%

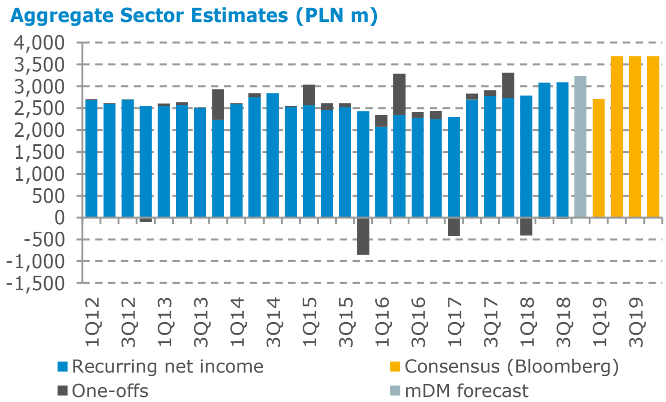
Source: Dom Maklerski mBanku

2018 Q4 earnings calendar

	Preliminary Results	Final Results
Santander	2019-01-31	2019-02-22
Millennium	2019-02-05	2019-02-22
Pekao		2019-02-26
mBank	2019-02-07	2019-02-27
Alior Bank		2019-02-28
PKO BP		2019-03-04
ING	2019-02-13	2019-03-08
BOŚ		2019-03-14
BGŻ BNP Paribas		2019-03-14
Handlowy	2019-02-14	2019-03-22
Getin Noble Bank		2019-04-26
Idea Bank		2019-04-26

Source: Banks

Historical and expected quarterly earnings



Source: Banks, Dom Maklerski mBanku, Bloomberg

The Champion: Pekao

Pekao is expected to come out as the top earner of Q4 2018, delivering superior earnings quality and composition, evidenced by strong income and reined-in costs. PKO BP will be a close second with its net profit topping the PLN 1 billion mark.

On the other hand, Millennium and Alior Bank might disappoint slightly with high integration costs and charge-offs of corporate loans. In case of Alior, by writing off a chunk of bad debt in Q4 the Bank would mitigate risk which would otherwise hand over its head throughout 2019.

2019 Dividend Expectations

Capital requirements for dividends, 2019E DPS

	75% payout ratio		100% payout ratio		Actual @31 Sep.'18		
	Tier 1	TCR	Tier 1	TCR	Tier 1	TCR	'19E DPS
PKO BP	14.3%	16.4%	15.0%	17.1%	17.1%	18.4%	1.49
Pekao	13.8%	15.8%	18.0%	20.0%	16.1%	17.0%	6.32
Santander	13.9%	16.0%	14.8%	16.9%	15.5%	17.6%	26.37
ING	13.5%	15.5%	16.8%	18.8%	14.4%	15.2%	3.41
Millennium	17.7%	21.3%	21.2%	24.7%	20.9%	22.9%	0.00
Handlowy	13.3%	15.3%	17.7%	19.7%	16.9%	16.9%	3.80
Alior Bank	13.0%	15.0%	14.5%	16.5%	12.1%	15.3%	0.00

Source: Banks, Dom Maklerski mBanku

We have updated our 2019 dividend expectations for the banks in our coverage universe based on 2018 financials and the latest mid-term dividend guidance issued by the market regulator, KNF. The solvency requirements that cap the 2019 dividend payout ratios have tightened with the addition of an extra capital buffer following KNF-led stress tests (the "stress -test" or "ST add-on").

With that said, none of our rated banks had met the criteria for 100% capital distributions even before the ST add-on, with the exception of Pekao, which had vowed to distribute 90% minimum of the 2018 profit as dividends in 2019 – a promise it cannot keep under the updated capital requirements, prompting us to cut the expected capital distribution from 90% to 75%. At the same time, Pekao has promised to update its future dividend policy so as to keep the payout ratio at or around 75% in 2020 and 2021.

Santander also stands out from the pack with its plan sweeten the pot of a 50% distribution from 2018 earnings with an extra payout from retained earnings, which stand roughly at PLN 1.5bn, to offer its shareholders a record-high total per-share gain of PLN 26.37. This provided the regulator signs off on the extra payout.

Otherwise, the upcoming dividend declarations by banks are not likely to produce major surprises.

Alior Bank

- Alior will report its fourth-quarter results on February 28th.
- We expect to see net income growth of 2.0% q/q and 0.7% y/y to PLN 176.4m, an estimate 13% below the Q4 market consensus implied by the average of the full-year forecasts tracked by Bloomberg.
- The difference is due to our assumption that Alior will book a PLN 80m one-time charge in Q4 related to the acquisition of the troubled newspaper distributor Ruch.
- Alior will deliver its 2018 FY lending targets after growing the loan volume at an annual rate of 10% and adding 5% quarter on quarter.
- On an increasing loan portfolio, NII is likely to grow +3.1% q/q and +10.8% y/y, resulting in a stable NIM.
- We forecast provisioning at ca. PLN 220m on a recurring basis and PLN 304m after one-time boosts. Cost of risk ~207bp.
- There will be a 3.5% q/q rise to PLN 425m in operating expenses which, however, in Q3 were reduced by a charge reversal.
- Additional provisioning for potential losses on the Ruch acquisition should be welcomed by the market and make investors more comfortable with their forecasts for 2019. Sill unresolved is the question of the potential misselling fine from the KNF.
- In short, Alior's Q4 report should get a positive response from the market given a growing loan portfolio and increasing interest income.

Alior Bank 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	727.3	805.7	3%	11%
Fee income	132.5	106.5	0%	-20%
Total income	1,028.2	1,054.3	4%	3%
Operating expenses	442.3	425.9	-4%	-4%
Provisions	240.5	304.3	22%	27%
Net income	175.2	176.4	2%	1%

Source: Dom Maklerski mBanku

Santander Bank Polska

- Santander Bank Polska ("Santander") will report its fourth-quarter results on Wednesday, January 30th, 2019.
- We expect a quarterly net profit of PLN 868.9m, up 75.5% from the previous quarter and 58.4% year over year.
- This is a 6.6% lower call than the current consensus forecast, which may or may not factor in a one-time gain from negative goodwill arising on the acquisition of Deutsche Bank Polska (DBPL) in November, estimated to have provided a one-time boost of PLN 400m to Q4 profits. On the other hand, post-merger integration of DBPL, and further rebranding, will generate additional costs of ca. PLN 25m in Q4.
- Due to the DBPL deal the 2018 Q4 financials are not comparable with prior periods.
- Without restating prior periods, we expect the quarterly net interest income to show a 7.9% increase on the previous quarter and an 11.2% rebound year-over-year at PLN 1,535m. The net interest margin is set to bounce back to 3.42% (NIM ex. DBPL will also have expanded from the prior-year period) after 14bp shrinkage registered in Q3.
- Fee income will show flat growth from the comparable year -ago base, but including DBPL it is likely to be 10% higher than in the prior-year and quarter-before periods.
- Operating expenses will increase 9.0% q/q and 14.5% y/y in Q4, due in a large part to rebranding and post-merger integration expenses.
- We anticipate risk reserves of PLN 283.5m as of 31 December 2018 after a 13% jump relative to September, implying quarterly cost of risk of 87bp (over average loans), and FY2018 yearly cost of risk of ca. 80bp, in line with guidance.
- The fourth-quarter earnings release alone is not likely to have much impact on Santander's stock price, but the subsequent call with analysts might, depending on whether Santander reiterates its commitment to distribute retained earnings (PLN 1.47bn) as dividends this year, and on the 2019 guidance as regards post-merger integration costs.

Santander Bank Polska 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	1,379.4	1,535.0	8%	11%
Fee income	515.4	567.4	10%	10%
Total income	1,951.8	2,010.3	8%	3%
Operating expenses	839.9	961.7	9%	14%
Provisions	212.9	283.5	13%	33%
Net income	549.0	868.9	75%	58%

Source: Dom Maklerski mBanku

Bank Handlowy

- Handlowy will report Q4 results on February 14th, 2019.
- We expect net income to come in at PLN 171.8m after rising 8.4% q/q and 5.2% y/y, an estimate 4.0% above the market consensus implied by the average of the full-year forecasts tracked by Bloomberg.
- Trading income is likely to be one of the major growth drivers of Q4 after rebounding 17% q/q and 13% y/y after successful deals in the bond market.
- NII will post a 1.9% rise vs. Q3, with NIM tightening by a narrow 5bp.
- We expect stable provisioning at PLN 21m and cost of risk at 41bp, coming largely from the retail portfolio.
- OPEX @PLN 282m will be 2% higher than in Q3, when Handlowy reversed a PLN 6m charge, after a 1% uptick from the prior-year period.
- Summing up, Handlowy might surprise on the upside with the Q4 figures. The main questions heading into 2019 are about the new strategy and whether the loan book can grow faster this year.

Handlowy 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	290.3	286.0	2%	-2%
Fee income	144.8	132.4	-2%	-9%
Total income	546.9	544.1	5%	-1%
Operating expenses	280.0	281.8	2%	1%
Provisions	38.4	20.6	7%	-46%
Net income	163.4	171.8	8%	5%

Source: Dom Maklerski mBanku

ING BSK

- ING BSK will report its fourth-quarter results on February 13th, 2019.
- We expect to see net income of PLN 404.0m after 6.6% q/q and 10.1% y/y upswings, landing just shy of the record quarterly result of PLN 407m posted in Q2 2016, propped up by a bumper payday from the Visa deal.

- Compared to the consensus estimate implied by 2018 FY analysts' forecasts tracked by Bloomberg, our estimate stands 4% lower.
- We see NII growth of 1.8% q/q and 9.4% y/y, and stable NIM of 2.90%, for Q4. Fee income may post a 9.2% surge on an annual basis, as well as rising 4.3% from Q3, when, however, the takings from fees were curbed by extra one-time costs.
- There should be no change in operating costs relative to Q3, but on a y/y basis opex might have jumped as much as 9.1%, driven by payroll.
- Provisioning in Q4 will be 4.0% higher q/q and 23.7% higher y/y. Cost of risk was probably stable between the end of September and December, but TTM CoR might have climbed to 55bp from 53bp in Q3.
- The fourth-quarter earnings release is not likely to have much impact on the market's view on ING, but it will give a foretaste of things to come in 2019, when we believe the Bank will deliver new all-time high profits on a quarterly basis.

ING BSK 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	895.2	978.9	2%	9%
Fee income	302.2	330.1	4%	9%
Total income	1,227.3	1,343.5	3%	9%
Operating expenses	528.5	576.4	0%	9%
Provisions	112.6	139.3	4%	24%
Net income	366.8	404.0	7%	10%

Source: Dom Maklerski mBanku

Bank Millennium

- Millennium will release preliminary fourth-quarter results on Tuesday, February 5th, 2019.
- We anticipate a quarterly net income of PLN 184.6m, down 7.8% from the previous quarter but up 2.8% on the year.
- Compared to the implied consensus estimate (Bloomberg), our estimate stands 6.8% lower.
- The November acquisition of the SKOK Piast credit union is not going to have much of an effect yet on Q4 results.
- Net interest income is set to show growth of 2.0% from Q3 and 6.3% year over year at a projected PLN 472.1m.
- NIM (over average assets) will have stabilized at 2.53% after a double-digit boost of 10bp registered during Q3.
- Noninterest income will likely post declines of 1.5% q/q and 3.7% y/y, while fee income will probably be flat q/q.
- At PLN 328.0m opex be up 4% from Q3 and 8% from Q4'17, driven by the acquisition of Societe Generale Poland and SKOK Piast, combined with continuing pay pressures.
- Provisioning likely increased by 12.5% q/q to a projected PLN 65.2m, resulting in cost of risk at ca. 49bp.
- Our fourth-quarter view suggests that Millennium's 2018 full -year earnings might narrowly miss the expectations of the market. With that said, not counting extra expenses related to M&A activity, the fourth-quarter figures, in particular the net interest margin, actually look quite healthy. Note that profits in the first two quarters of 2019 will be weighed down by post-merger integration costs.

Millennium 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	443.9	472.1	2%	6%
Fee income	169.4	163.5	0%	-3%
Total income	685.5	704.7	1%	3%
Operating expenses	304.5	328.0	4%	8%
Provisions	63.0	65.2	12%	4%
Net income	179.6	184.6	-8%	3%

Source: Dom Maklerski mBanku

Pekao

- Pekao will report its fourth-quarter results on February 26th, 2019.
- We expect net income to come in at PLN 672.8m after rising 11% q/q and 36.2% y/y,
- Compared to the consensus estimate implied by 2018 FY analysts' forecasts tracked by Bloomberg, our estimate stands 1% lower.
- Like in the comparable prior-year quarter, Q4 financials will be propped up by one-time gains on NPL divestment.
- In terms of core business, we expect to see net interest income growth at a quarterly rate of 3.2% and an annual rate of 9.0%, and we anticipate flat NIM of 2.74%.
- This alongside flat q/q fee income.
- Risk reserves will have an ending balance of ca. PLN 150.6m, and cost of risk will be 42bp.
- Pekao's will be among the best Q4 showings in the financial sector, demonstrating strong revenue growth and tightly-managed expenses which make the bank a reliable bet for the coming periods.

Pekao 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	1,190.2	1,298.0	3%	9%
Fee income	617.2	620.5	0%	1%
Total income	2,001.4	2,059.0	5%	3%
Operating expenses	784.1	788.2	1%	1%
Provisions	152.8	150.6	-3%	-1%
Net income	1,054.1	672.8	11%	-36%

Source: Dom Maklerski mBanku

PKO BP

- PKO BP will release its fourth-quarter results on March 4th, 2018.
- At PLN 1,000.9m, net income will have tightened 4% from Q3 after a y/y jump of 22%.
- Compared to the consensus estimate implied by 2018 FY analysts' forecasts tracked by Bloomberg, our estimate stands 4.7% higher.
- We see quarterly growth of 2.6% and y/y expansion of 8.0% to PLN 2.43bn in net interest income, with NIM holding at a stable 3.14%.
- Anticipating a 4% rise in other noninterest income and flat growth in fee income.
- Payroll will be responsible for the bulk of the expected 1.7% seasonal surge in operating expenses.
- Risk reserves will have decreased 13% relative to the year-ago period at a projected PLN 389m. Cost of risk at 70bp broadly consistent with the 2018 ytd average of 66bp
- The effective tax rate for Q4 will be seasonally high at 23.6%.
- We expect a positive reaction to the Q4 results as the market notices strong interest income and slightly-curbed operating expenses, and recognizes PKO's potential to grow earnings at double-digit rates in FY2019.

PKO BP 2018 Q4 estimates

(PLN m)	Q4'17	Q4'18	Q/Q	Y/Y
Net interest income	2,249.0	2,428.7	3%	8%
Fee income	760.0	759.5	0%	0%
Total income	3,339.0	3,545.9	3%	6%
Operating expenses	1,474.0	1,465.6	1.7%	-1%
Provisions	448.0	389.0	19%	-13%
Net income	820.0	1,000.9	-4%	22%

Source: Dom Maklerski mBanku

List of abbreviations and ratios contained in the report.
EV – net debt + market value (EV – economic value)
EBIT – Earnings Before Interest and Taxes
EBITDA – EBIT + Depreciation and Amortisation
PBA – Profit on Banksng Activity
P/CE – price to earnings with amortisation
MC/S – market capitalisation to sales
EBIT/EV – operating profit to economic value
P/E – (Price/Earnings) – price divided by annual net profit per share
ROE – (Return on Equity) – annual net profit divided by average equity
P/BV – (Price/Book Value) – price divided by book value per share
Net debt – credits + debt papers + interest bearing loans – cash and cash equivalents
EBITDA margin – EBITDA/Sales

OVERWEIGHT (OW) – a rating which indicates that we expect a stock to outperform the broad market
NEUTRAL (N) – a rating which indicates that we expect the stock to perform in line with the broad market
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Economic profits – discounting of future economic profits; the weak point is high sensitivity to changes in the assumptions made in the valuation model.
Discounted Dividends (DDM) – discounting of future dividends; the weak point is high sensitivity to changes in the assumptions as to future dividends made in the valuation model.
NAV - valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

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