

Wednesday, June 26, 2019 | update

## PKO BP: accumulate (reiterated)

PKO PW; PKO.WA | Banks, Poland

### Quality and dividend

We keep our Accumulate recommendation for PKO BP unchanged and raise the target price to PLN 47.17. In our opinion, PKO BP's recent results represent above-average quality. The Company's reported results have been in line with or above market expectations for nine consecutive quarters. In view of high growth in net interest income supported by retail loan sales and high quality of the portfolio, we have upgraded our forecasts by 7% for 2019 and 5%-6% for the next two years. The 2019 results should include additional PLN 235m one-off gains on the reversal of withholding taxes (1Q'19), the recognition of badwill on the acquisition of PCM (2Q'19) and the revaluation of interests in PSP – BLIK (3Q'19). Our projection includes a dividend payout from undivided earnings and a rerun of that scenario in 2021. In our opinion, PKO BP's capital adequacy ratios allow for such payments, additionally encouraged by the emerging Prime Minister's "Capital Investment Fund" to be formed with dividends paid by government-owned companies. In our view, the high dividend and the growing profitability merit PKO BP's rating to 13.0x fair P/E.

### Upgraded forecasts

We have upgraded our forecasts by 7% for 2019 and 5%-6% for the next two years. The upgrade results from a stronger outlook of the net interest income (a higher net interest margin) combined with lower cost of risk which have been a steady surprise in the last two years (except 4Q'18). In our opinion, the net profit mark of PLN 5bn is unlikely to be crossed before 2022, which we believe is the bank's unofficial target. Our forecasts are 7% above the 2019 consensus and 2%-3% above the 2020-21 consensus.

### DYield to put dividend-paying stocks to shame

In our opinion, PKO BP's capital position allows for the payout of approx. 100% of net profits in the next two years (50% of last year's earnings + 50% of undivided earnings for the previous years), which would imply a DYield of 7%-9%. The payout may also be encouraged by the formation of a Capital Investment Fund to be managed by the Prime Minister and built up with dividends paid by government-owned companies. In our opinion, the key risks to our dividend projection include PKO BP's asset acquisitions, which seems like a rather remote prospect.

### Re-rating to continue

The strong 1Q'19 results and a potentially higher dividend have triggered a sudden rerating of PKO BP. While PKO's 12M fwd P/E hit this year's low of 11.2x on 11 May, it has since risen to 12.8x. Interestingly, Fair P/E remains in a downtrend, which could be a harbinger of a virtual avalanche of analyst reratings. Our 2020 Fair P/E is 13.0x, at a small discount to ING BSK, which still implies potential 10% growth.

(PLN m)	2017	2018	2019E	2020E	2021E
Net interest income	8 606.0	9 353.0	10 289.7	10 975.3	11 615.6
Non-interest income	4 220.0	4 307.0	4 353.6	4 413.7	4 543.2
Total operating expense	6 050.0	6 218.0	6 420.9	6 552.7	6 731.3
Operating profit	6 776.0	7 442.0	8 222.4	8 836.3	9 427.5
Net income	3 104.0	3 741.0	4 408.8	4 550.7	4 833.3
Cost/income (%)	47.2	45.5	43.8	42.6	41.7
ROE (%)	9.0	9.9	10.9	10.7	11.0
P/E (x)	17.0	14.1	12.0	11.6	10.9
P/BV (x)	1.5	1.3	1.3	1.2	1.2
DPS	0.00	0.55	1.50	3.10	3.75
Div. Yield	0.0	1.3	3.5	7.3	8.9

\*before provisions

Current Price	PLN 42.20
Target Price	PLN 47.17
Market Cap	PLN 52.75 bn
Free Float	PLN 37.23 bn
ADTV (3M)	PLN 176.9 ml

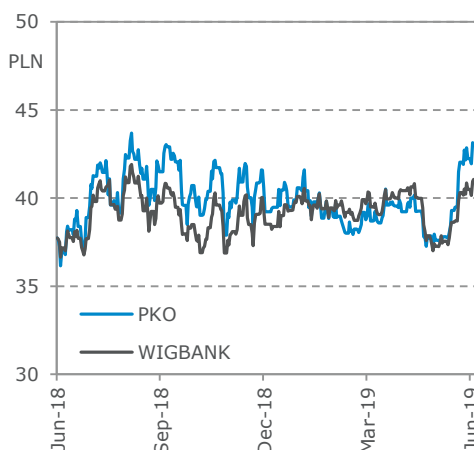
### Ownership

State Treasury	29.43%
NN OFE	7.64%
Aviva OFE	7.13%
Others	55.80%

### Company profile

The Bank holds Poland's biggest retail and corporate deposit and loan portfolio. It has a well-balanced balance sheet and high capital adequacy ratios. It holds 99.6% of Ukrainian Kredobank, which represents approx. 1% of the group assets.

### PKO vs. WIG Banks



Company	Target Price		Rating	
	new	old	new	old
PKO BP	47.17	40.92	accumulate	accumulate

Company	Current Price	Target Price	Upside/Downside
PKO BP	42.20	47.17	+11.8%

Forecast revision since last update	2019E	2020E	2021E
EBITDA	+0.7%	+0.5%	-0.1%
Pre-tax profit	+5.8%	+4.6%	+5.7%
Net profit	+6.7%	+4.8%	+6.2%

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**List of abbreviations and ratios contained in the report:**

**EV** – net debt + market value  
**EBIT** – Earnings Before Interest and Taxes  
**EBITDA** – EBIT + Depreciation and Amortisation  
**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  
**UNDERWEIGHT (UW)** – a rating which indicates that we expect the stock to underperform the broad market

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**HOLD** – we expect that the rate of return from an investment will range from -5% to +5%  
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**Relative** – based on a comparison of valuation multipliers of companies from a given sector; simple in construction, reflects the current state of the market better than DCF; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.

**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.



**mBank issued the following investment recommendations for PKO BP in the 12 months prior to this publication**

<b>Rating</b>	<b>accumulate</b>	<b>hold</b>	<b>accumulate</b>	<b>buy</b>	<b>accumulate</b>
Rating date	2019-05-09	2019-02-01	2018-12-05	2018-11-05	2018-10-04
Target price (PLN)	40.92	40.92	45.00	47.00	47.00
Price on rating day	37.78	39.51	41.96	40.39	42.55

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