

Wednesday, July 31, 2019 | special comment

Erste Group – Q2 Financials Signal Beat On FY Consensus

Rating: buy | target price: EUR 43.72 | current price: EUR 33.20

EBS AV; ERST.VI | Banks, Austria

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- Erste Group generated **net income** of EUR 354.9m in Q2 2019, representing 5.8% contraction from the previous quarter and a 19.0% fall from the same year-ago period which, however, can be mostly attributed to non-recurring events including a EUR 150.8m provision related to a lost legal case in Romania.
- Attr. net income showed a 4% miss vis-à-vis our estimate despite a 4% beat on pre-tax income due to an effective tax rate of 20% vs. 19% expected by us, combined with 30% higher-than-forecast minority interest.
- Net interest income** grew 0.7% q/q and 3.3% y/y in Q2 2019, but NIM stayed flat at 2.18% after an improvement in Romania (+14bp q/q) was offset by a deterioration in Hungary (-8bp q/q) and Croatia (-5bp).
- Operating costs** came out slightly below market expectations after decreasing 7.6% from Q1, when Erste booked one-time charges; relative to Q2 2018 OPEX was up 1.9% on the back of higher payroll and marketing expenses.
- Erste recognized **net reversals** of EUR 7m in Q2 2019 contrary to expectations of EUR 9m charge-offs. The biggest reversals in the period were booked in Romania (EUR 10m), Hungary (EUR 10m), and Austria (-EUR 8m), against higher lease-related charge-offs reported in Slovakia (+EUR 16m in Q2 vs. EUR 2m in 1Q'19).
- Erste has **reiterated its FY2019 guidance** which puts target ROTE above 11% (assuming an effective tax rate below 20%), assumes revenues will increase faster than costs, and aims to grow the loan portfolio in the mid-single digits. At the same time, the 2019 cost-of-risk guidance has been reduced from the 10-20bp range to 10bp or less. The underlying economic assumptions include GDP growth at 3%-4% in the core CEE markets and 2% in Austria.
- Erste delivered a set of very healthy 2019 Q2 results, fulfilling 48% of the FY2019 consensus forecast and 49% of our forecast in the first half of the year, which, however, is seasonally the slower half due to a range of yearly expenses and one-time charges that the Bank was required to pay (incl. contributions into the resolution fund and bank taxes, this year additionally boosted by the legal costs in Romania). Based on ytd results, the current market consensus looks underestimated by as much as 11%. Erste Group is currently trading at more attractive multiples than any other bank in our coverage universe.**

2019 Q2 earnings call:

Date: 31 July 2019

Time: 9:00 a.m. (CET)

T:44 (0)330 336 9126

Confirmation Code: 2198687

Summary of Q2 2019 results

(EUR m)	Q2'18	Q1'19	Q2'19	Y/Y	Q/Q
Net interest income	1,131.2	1,160.9	1,168.8	3.3	0.7
Fee income	480.7	487.7	492.7	2.5	1.0
Trading income	56.9	78.5	117.4	106.2	49.5
Total income	1,668.8	1,727.1	1,778.9	6.6	3.0
Operating income	2.6	-46.6	-141.7	n.m.	203.8
Bank tax	-24.7	-38.8	-25.9	4.6	-33.4
Operating expenses	-1,011.5	-1,115.6	-1,030.4	1.9	-7.6
Operating income before provisioning	635.2	526.0	580.9	-8.5	10.4
Provisioning	18.9	35.8	7.1	-62.5	-80.2
Pre-tax income	654.0	561.8	588.0	-10.1	4.7
Tax	-120.4	-95.5	-117.2	-2.6	22.7
Net income from discontinued operations	0.0	0.0	0.0	n.m.	n.m.
Net income	533.6	466.3	470.8	-11.8	1.0
Minority interests	-95.4	-89.3	-115.9	21.5	29.7
Net income attr. to owners of the parent	438.2	377.0	354.9	-19.0	-5.8

Source: Erste Bank, E - estimates by Dom Maklerski mBanku, Consensus estimates provided by Bloomberg

2019 Q2 actuals vs. expectations

(EUR m)	Q2'19	Consensus	differ.	Q2'19E	differ.
Net interest income	1,168.8	1,187.0	-1.5%	1,174.8	-0.5%
Fee income	492.7	494.2	-0.3%	497.4	-1.0%
Operating costs	-1,030.4	-1,041.2	-1.0%	-1,026.4	0.4%
Provisioning	7.1	-8.5	-	7.2	-1.2%
Net profit	354.9	328.0	8.2%	368.9	-3.8%

Source: Erste, E - estimates by Dom Maklerski mBanku, Consensus estimates provided by Bloomberg

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 Banking 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
UNDERWEIGHT (UW) – a rating which indicates that we expect the stock to underperform the broad market

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