

Monday, October 28, 2019 | special comment

## Millennium Bank - Q3 Consensus Beat But Core Business Disappoints

Rating: reduce | target price: PLN 5.18 | current price: PLN 5.83

**MIL PW; MILP.WA | Banks, Poland**

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- Millennium generated **net income** of PLN 200.1m in Q3 2019, representing a 15.3% rebound from the previous quarter and flat growth from the comparable year-ago period.
- The bottom-line figure **topped the average market estimate** (PLN 179.0m), and came ahead of our PLN 179.9m forecast, but the beat was owed solely to a PLN 45m gain on revaluation of the Bank's investment in the BLIK mobile payments solution.
- The third quarter was the first full quarter of results since the Eurobank acquisition. Other nonrecurring events affecting Q3 figures included post-merger **integration costs** in the amount of PLN 44.3m (making for a ytd total of PLN 64m), additional loan loss **provisions** in the amount of PLN 8m associated with Eurobank's loans, and an **initial reserve for potential fee refunds** on consumer loans repaid prematurely (PLN 53m total, of which PLN 21m charged against net interest income and PLN 32m booked under other costs).
- Net loans** increased by 2.3% Q/Q in the third quarter, driven mainly by consumers (+3%). Compared to the previous quarter, sales of payday loans fell 7% while mortgage lending was up by 9%. Sales of leased assets decreased by 17%, and factoring was down 3%.
- Net interest income** rebounded at a rate of 20% relative to Q2 and 49% year-over-year, landing just 1% above the consensus estimate and matching our forecast. The PLN 21m charge against NII related to potential cost refunds to early loan payers under a September ruling by the European Court of Justice is set to recur in future quarters.
- Fee income** expanded by 2% Q/Q and 9% Y/Y, supported by Eurobank contributions, with the quarter-on-quarter growth led mainly by higher loan fees (+14%).
- Operating expenses** went up by 29% Q/Q and 52% Y/Y due to the Eurobank merger and its subsequent integration, with the related costs increasing to PLN 44.3m from PLN 17.8m in Q2. Other opex also included a PLN 32m reserve for potential early loan fee refunds.
- Provisioning** decreased by 14% q/q in Q3, but the ending balance was higher than forecast by the market after additional charges of PLN 8m booked in connection with the loan book of Eurobank (down from PLN 80.6w in Q2). Millennium **significantly increased provisioning for retail loans** in Q3 to PLN 114m from PLN 58m the previous quarter.
- The **Total Capital Ratio** (incl. net income in the amount of PLN 334m) as of 30 September was 20.2%, and the **Tier 1 ratio** stood at 17.1%.
- We are slightly disappointed by the quality of Millennium's 2019 Q3 earnings, most notably by the one-time boost to the quarterly net income coming from a deal which has only been closed in October. We are also rather let down by the slow pace of lending growth aside from mortgages, and by high costs of risk in retail. Going forward, it looks like the Bank's quarterly profits will be weighed down by recurring provisions for potential early loan refunds and by costs of post-merger integration, on top of the looming costs of FX mortgage lawsuits now that the CJEU has given its verdict. We currently have a reduce recommendation for MIL.**

### Q3 Earnings Conference Details:

Date: 28 October 2019

Time: 2:00 p.m. (CET)

Venue: Warsaw, ul. Stanisława Żaryna 2A

Webcast link: <http://infostrefa.tv/millennium/en>

### 2019 Q3 actuals vs. expectations

| (PLN m)             | Q3'19  | consensus | Differ. | Q3'19E | Differ. |
|---------------------|--------|-----------|---------|--------|---------|
| Net interest income | 687.6  | 694.3     | -1.0%   | 688.0  | -0.1%   |
| Fee income          | 178.3  | 176.5     | 1.0%    | 178.5  | -0.1%   |
| Operating costs     | -480.1 | -485.4    | -1.1%   | -490.5 | -2.1%   |
| Provisioning        | -133.8 | -130.8    | 2.3%    | -127.0 | 5.3%    |
| Net income          | 200.1  | 179.0     | 11.8%   | 179.9  | 11.2%   |

Source: Millennium, E - estimates by Dom Maklerski mBanku; Consensus estimates provided by PAP

**Overview of 2019 Q3 results**

| (PLN m)                                | Q3'18        | Q2'19        | Q3'19          | Y/Y (%)     | Q/Q (%)     |
|--|--------------|--------------|----------------|-------------|-------------|
| <b>Net interest income</b>             | <b>463.0</b> | <b>572.5</b> | <b>687.6</b>   | <b>48.5</b> | <b>20.1</b> |
| Fee income                             | 162.9        | 175.0        | 178.3          | 9.4         | 1.9         |
| Trading income                         | 64.2         | 77.7         | 113.9          | 77.3        | 46.6        |
| Other income                           | 9.7          | 12.1         | 28.5           | 192.2       | 134.3       |
| <b>Non-interest income</b>             | <b>236.9</b> | <b>264.9</b> | <b>320.7</b>   | <b>35.4</b> | <b>21.1</b> |
| <b>Total income</b>                    | <b>699.9</b> | <b>837.4</b> | <b>1 008.3</b> | <b>44.1</b> | <b>20.4</b> |
| Operating expenses                     | 316.0        | 371.6        | 480.1          | 51.9        | 29.2        |
| Other costs                            | 13.1         | 17.8         | 56.9           | 334.0       | 220.0       |
| <b>Total costs</b>                     | <b>329.1</b> | <b>389.3</b> | <b>537.0</b>   | <b>63.1</b> | <b>37.9</b> |
| <b>Operating income</b>                | <b>370.7</b> | <b>448.1</b> | <b>471.3</b>   | <b>27.1</b> | <b>5.2</b>  |
| Provisions                             | 58.0         | 154.9        | 133.8          | 130.9       | -13.6       |
| Equity in profits/losses of associates | 0.0          | 0.0          | 0.0            | n.m.        | n.m.        |
| <b>Pre-tax income</b>                  | <b>312.8</b> | <b>293.2</b> | <b>337.5</b>   | <b>7.9</b>  | <b>15.1</b> |
| Tax                                    | 64.7         | 60.9         | 68.5           | 5.9         | 12.6        |
| <b>Net income</b>                      | <b>248.1</b> | <b>232.3</b> | <b>269.0</b>   | <b>8.4</b>  | <b>15.8</b> |
| Bank tax                               | 47.9         | 58.7         | 68.8           | 43.8        | 17.4        |
| <b>Net income after bank tax</b>       | <b>200.2</b> | <b>173.7</b> | <b>200.1</b>   | <b>0.0</b>  | <b>15.3</b> |

Source: Millennium, 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 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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**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.

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