

FIRST INVESTMENT BANK IPO

General Information

The IPO of First Investment Bank (FIB) should become the largest in Bulgaria. The capital will be increased by 10 million shares and in addition, the shareholder First Financial Brokerage House will offer up to 6.5 million shares. At the estimated prices between BGN 8 and BGN 11, the IPO could exceed BGN 150 million. The period of subscription is between the 7th and the 18th of May, but this will ease the procedure for small orders as large investors will wait the end of the period. The banking sector is usually attracting broad investment interest as it is representative for the development of the economy and the consumer demand. After the solid oversubscription of Corporate Commercial Bank (CTB) of more than 13 times for market orders and 6 times for limit orders at the maximum price, we expect strong demand for the shares of FIB too.

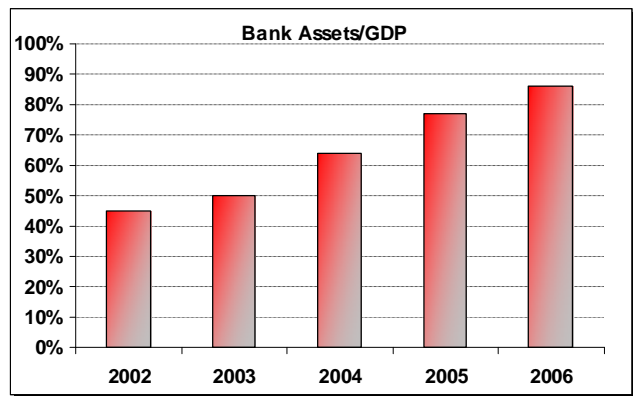
Bulgarian Banking Sector

The banking sector's assets are rising faster than the nominal GDP, thus moving to 86% of GDP last year. This ratio is still low as compared to EU countries and is the main reason for the strong growth in the sector.

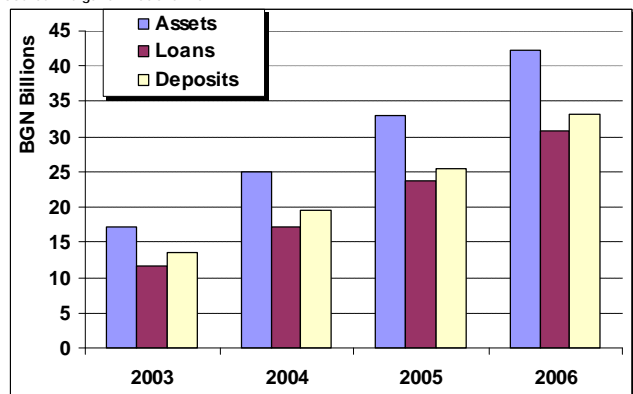
2006 brings two interesting observations. The first is the decelerating growth of loans to non-financial institutions (NFI), which fell below the growth rates of total loans, assets and deposits. At the same time, deposits rose faster than assets and more important, faster than loans to NFI. The credit growth during 1Q 2007 is accelerating again with corporate loans leading the charge.

The new tendency of faster growth of deposits is changing the banking environment. The excess growth of deposits is pressuring down the net interest income of retail banks. As long as the bad loans maintain their low levels, the Central Bank will allow faster credit growth like the solid increase in 1Q 2007. Banks with faster credit growth and popularity among clients have better perspectives in mid-term.

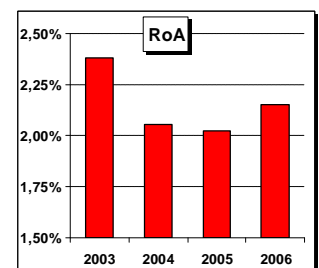
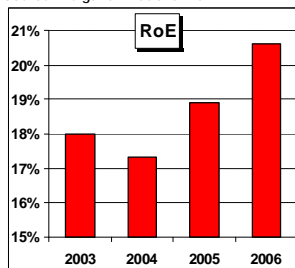
The banking sector enjoyed a long period of rising profits and revenues from interest and fees. This won't continue indefinitely. The average RoE for Bulgarian banks is 20.61% and the indicator is close to the sector average in Central and Eastern Europe. The jump of assets in 2004 (44%) resulted to the decrease of RoE but the following years showed solid improvement.



Source: Bulgarian National Bank



Source: Bulgarian National Bank



Average values for Assets and Equities. Source: Bulgarian National Bank. Calculations: ELANA Trading

IPO Procedure and Timeframe

FIB will increase its capital from 100 million shares to 110 million. In addition, the shareholder and leading manager of the IPO First Financial Brokerage House will offer for sale 5 million existing shares and up to 1.5 million depending on the oversubscription. No price range is set but the leading manager of the IPO is expecting a range between BGN 9 and BGN 10 and two times oversubscription, according to the feedback from institutional investors.

The price and the allocation proportion will be determined by the conditions of book-building and will be equal for all participants. The leading manager will provide stabilization of the price in the first 30 trading days. The lock-up period is six months after the offering.

Shareholders' Structure

The shareholders with largest stakes before the IPO are the founders of the bank. Mr. Ivailo Mutafchiev and Mr. Tseko Minev have 31.83% each, and First Financial Brokerage House owns 13.89%. During the years, among the shareholders were also the investment fund EPIC and EBRD. The latter sold its stake of 20% in December 2005. Other shareholders are the Cyprus Legnano Enterprise (8.45%) and the British Virgin Islands Domenico Ventures (7%) and Rafaela Consultants (7%).

Business Description

First Investment Bank is the 5th largest Bulgarian bank in terms of assets and is struggling to maintain its market position with foreign-owned institutions. FIB is the largest domestically owned bank which provides universal banking services through wide branch network. The institution was created in 1993 and received its license from the Central Bank in 1997. Initially, FIB provided services to corporate clients but gradually broadened its services to individuals.

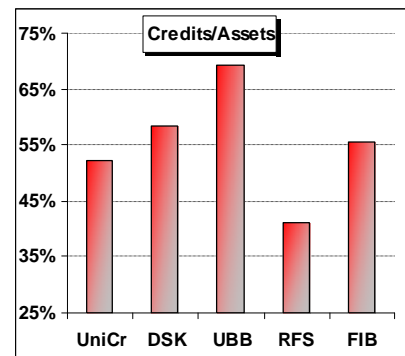
FIB is the third largest corporate lender with 9% market share of bank loans to non-financial institutions. This is substantially higher than the market share of 7.5% in terms of assets but FIB's positions in other segments are lower. The bank's market share in the segment of consumer and mortgage loans is 4.7% and 6.7%, respectively. Credits represent 55% of total assets of FIB, which is close to the average level for the five largest banks in Bulgaria.

The structure of the credit portfolio of FIB showed that the bank has the lowest level of consumer (12.38%) and mortgage loans (13.38%) to total loans among the five largest players. Commercial loans represent 70% of the total loans to non-financial institutions. This specialization is not unique in top 5; in fact, Unicredit (UniCr) and Raiffeisen Bank (RFS) also maintain their focus to corporate loans. FIB's growth rate of loans is faster than the average for the banking system.

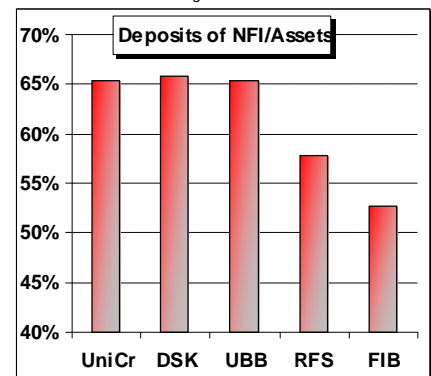
FIB has deposits of NFI to assets ratio of 53% which is below the average for the banking system and for the top 5 largest banks. This is showing the importance of bonds, syndicated loans and repurchase agreements. However, the corresponding price is higher than the deposits' rates.

Deposits by individuals are 61% of total and are growing by 45% annually for the last three years. The average rate paid on liabilities is 4.31% in 2006. Rising deposits are behind the lower interest costs but the improved risk premium of FIB also contributed, despite the higher EURIBOR.

Several refinancing operations in 2008 should improve further the average rate paid on liabilities. The total costs to revenues are falling due to the higher scale of operations.



Source: Bulgarian National Bank, as of end-2006
Data for Unicredit are cumulative for Bullbank, HVB Biochim and Hebros Bank
Calculations: ELANA Trading



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Business Description

FIB is maintaining a fast growth of assets. However, the astonishing 52.80% in 2005 was followed by 25.05% in 2006. The restrictions of the credit expansion by the Bulgarian National Bank had a negative impact on loans. As a result, FIB's growth decelerated below the average for the banking system in 2006 (28.44%).

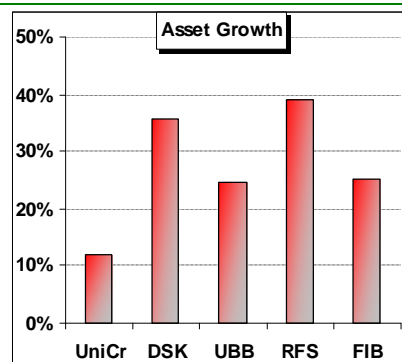
This had a positive effect on the profitability ratios. The return on average equity improved to 19.69% in 2006 from 17.43% a year earlier. The return on average assets increased to 1.05% in 2006 from 0.90% in 2005 but is still below the 1.32% RoA in 2004.

Moreover, the necessity of new capitals also decreased. The growth of deposits (40.9% in 2006) was sufficient to support the assets increase. Deposits have lower costs as compared to the other sources of capitals.

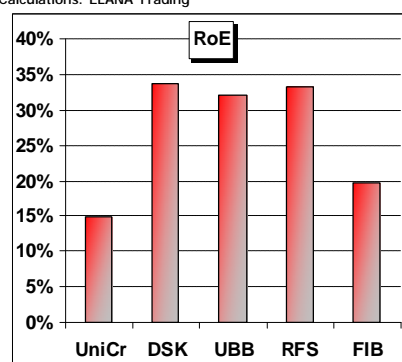
The bank is using subordinated debt and hybrid capital instruments to increase its equity, along with the retained earnings. The subordinated debt and hybrid capital instruments are used in the calculation of the capital adequacy requirements and were the primary tools to support the assets' growth.

The 2006 proved that the *growth at all cost* is not the best strategy for FIB. The capital increase will provide a cheap financing as compared to the bonds and hybrid capital instruments. The bank is planning to maintain its position as 5th largest bank with 8% market share in 2008. The expected RoA is above 2% as well as RoE of 23% for 2009. This is requiring not only better revenues to costs ratio but also the decrease of average rate paid on debt instruments.

The bank's credit rating assigned by Moody's is Ba3 /positive/ and by Fitch is BB- /positive/.



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Capital Adequacy

The capital adequacy ratio for 2006 is 13.05% or an increase from the 13.96% for 2005. The average for the banking system in 2006 is 14.50% and the required ratio for Bulgarian banks is 12%.

The risk exposure is close to the average for the banking system. Watch credits are 1.26% of total credits in 2006, whereas substandard and non performing loans are 3.6%. Part of watch credits in 2005 (4.87%) passed over the other categories as they totaled 1.89% in 2005.

Financial Situation and Projections

BGN '000	2004	2005	2006	2007f	2008f	2009f
Assets - end of period	1 651 119	2 522 983	3 155 046	3 734 000	4 377 000	5 382 000
Average Assets	1 336 723	2 330 928	2 733 118	3 444 523	4 055 500	4 879 500
Equity - end of period	108 429	129 628	168 350	300 400	379 026	473 148
Average Equity	102 603	120 610	145 975	234 375	339 713	426 087
Net Profit	17 620	21 018	28 747	45 000	71 000	98 000
RoE	17,17%	17,43%	19,69%	19,20%	20,90%	23,00%
RoA	1,32%	0,90%	1,05%	1,31%	1,75%	2,01%

Forecasts from FIB and FFBH

Valuation

The price for the IPO will depend on the received orders and the memorandum didn't provide either minimum or maximum price. However, the leading manager expects price range between BGN 9 and 10 per share. The first quarter financial statement is a positive step toward the implementation of the projected targets for assets, RoA and net profit. Assets decrease but the net interest income improved as compared to year ago and to the previous quarter.

We extended the indicative range from BGN 7.50 to 12.00 to represent all possible trailing P/E and P/B ratios. The comparison with Central and Eastern Europe banks showed average P/B of 4. The average P/E is below 25 for Poland, Hungary and Czech Republic but the faster growing markets like Bulgaria, Romania and Croatia are trading at higher multiples.

The low level of the indicative range (BGN 9) provide us with comfort as the trailing P/E is 30 but the book value of 3.70 looks attractive as compared to other Bulgarian banks.

The assumptions of 20% asset growth in 2007 and improved RoA of 1.30% are used for the calculation based on the forward P/E. The calculated net profit for 2007 is almost equal to the estimated by the management. However, we use forward P/E of 20 to incorporate the risk of negative surprises, which result into price of BGN 8.20. The sensitivity analysis extends the calculations to forward P/E of 24 and better return on average assets.

The market will tolerate higher P/E ratio in exchange of level of 4 for P/B. This is the reason to expect the price between BGN 9.50 and 10.00 for the IPO. The source of cheap capital for the bank should improve the profitability of the bank in medium to long term.

Valuation Based on Trailing P/E and P/B

Price	P/E	P/B	Price	P/E	P/B
7,50	24,65	3,26	10,00	32,87	3,95
8,00	26,29	3,41	10,50	34,51	4,08
8,50	27,94	3,55	11,00	36,15	4,20
9,00	29,58	3,69	11,50	37,80	4,31
9,50	31,22	3,83	12,00	39,44	4,43

1Q 2007 data are used for the calculation of P/E and P/B with the presumption of full subscription of new shares on the IPO.

Calculations: ELANA Trading

Valuation Based on Forward P/E

BGN '000	
Asset Growth	20,00%
Assets - end of period	3 786 055
Average Assets	3 470 551
RoA	1,30%
Expected Net Profit	45 117
Expected Forward P/E	20,00
Calculated Market Cap	902 343
Number of Shares	1 10 000 000
Price per Share (BGN)	8,20

Calculations: ELANA Trading

Sensitivity Analysis

		RoA				
		1,20%	1,25%	1,30%	1,35%	1,40%
Forward P/E	17	6,44	6,70	6,97	7,24	7,51
	18	6,81	7,10	7,38	7,67	7,95
	19	7,19	7,49	7,79	8,09	8,39
	20	7,57	7,89	8,20	8,52	8,83
	21	7,95	8,28	8,61	8,94	9,28
	22	8,33	8,68	9,02	9,37	9,72
	23	8,71	9,07	9,43	9,80	10,16
	24	9,09	9,47	9,84	10,22	10,60

Calculations: ELANA Trading

One Year Price Target

The one year price target is calculated through the P/E of 25 and the expected net profit, as well as the P/B of 4 and the equity of BGN 300 million. Both targets are above the guidelines for the IPO price range. P/E of 25 and P/B of 4 are lower than the current for listed Bulgarian banks. We are reluctant to give higher values as FIB is larger bank and should have better liquidity and significant free float.

The liquid Bulgarian stocks are traded at levels of 25 P/E or above for the last several quarters and we expect that similar values for multiples will be common for the market in mid-term perspective.

BGN '000	
Net Profit	45 117
P/E	25,00
Calculated Market Cap	1 127 929
Price per Share (BGN)	10,25
Equity	300 400
P/B	4,00
Calculated Market Cap	1 201 600
Price per Share (BGN)	10,92

Calculations: ELANA Trading

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Outperform	More than 5% higher as compared to SOFIX and BG40 performance
Market Perform	Market performance, +/-5% as compared to SOFIX and BG40
Underperform	More than 5% lower as compared to SOFIX and BG40 performance

Frequency of Recommendations: No schedule of recommendations is available. The frequency of recommendations depends on specific factors to individual companies and the opinion of the analyst(s) for the necessity of minor or major changes.

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