



Stock Price of First Investment Bank



- First Investment Bank (5F4) remains among the fastest growing Bulgarian banks, but the growth rate of its assets has slowed down substantially this year. This is due to the higher base for each year, although the drop in interest rates also leads to weaker demand for the bank's deposits. It has to be noted that FIB has decreased the expenditure on interest as a percentage of attracted funds less than the banking system's average. We expect the bank to continue increasing its assets.

- During the third quarter deposits rose by 18%, which is the lowest rate for the last two years. As a result there is a permanent decrease in equity, with an equity-to-assets ratio of 7.37%. This level is much lower than the average for the banking system and shows the need of capital increase. Shareholders will adopt at an extraordinary meeting an amendment in the Statute, which will allow the Management Board to initiate a procedure for capital raise. It is expected that this will happen in 2013. Recently the bank issued hybrid debt to improve its capital adequacy.

- The profit margin has fallen compared to last year. Income gained from financial instruments during the third quarter is large, which compensates for the increase of the impairment to 11.3 million BGN. FIB reported a slight improvement in the net interest margin due to the steady reduction of costs for attracted funds. The bank showed a seasonal increase in the income from fees and commissions as a percentage of assets during the third quarter.

- Financial assets have decreased as a nominal value by BGN 100 million, but the growth in cash and cash equivalents was twice higher. The bank's loans have increased by 150 million BGN during the third quarter, but remained at the 69% level of the bank's assets.

- The bank has not announced the level of bad debt in its unconsolidated report at the end of the third quarter. As of the middle of 2012, 15.41% of the gross loan portfolio of FIB was classified as non-performing.

- Shares of the bank have fallen to the lowest level in the last three years, which is due to the expected increase in equity. The worsening of yearly profits during the third quarter also played a role in the sale of stock. We expect that the decline will be in low volumes, mainly due to the sell-off of domestic speculators as the usual demand has been withdrawn.

Valuation

We compare the multiples of the three largest public listed banks in Bulgaria with the medians for Eastern Europe. The price-to-earnings ratios of the three banks with positive profits are calculated based on the unconsolidated results for the last twelve months. We give 40% weight of P/B and P/E ratios, whilst price-to-assets have a weight of 20%, which accounts for the lower importance of the size of the financial institution compared to the profitability.

*Table 1
Multiples
valuation*

	Central Cooperative Bank	Corporate Commercial Bank	First Investment Bank
Number of Shares	113 155 092	6 000 000	110 000 000
Price-to-earnings of peers	9.31	9.31	9.31
Net Profit (ttm)	10 413 000	45 545 000	28 837 000
Target price	0.86	70.68	2.44
Price-to-book of peers	0.58	0.58	0.58
Equity	343 424 000	414 939 000	499 034 000
Target price	1.76	40.10	2.63
Price-to-assets of peers	0.07	0.07	0.07
Assets	3 250 417 000	5 069 752 000	6 772 376 000
Target price	1.87	55.11	4.02
Fair Price	1.42	55.34	2.83
Current Price	0.58	79.00	1.36
Premium (Discount)	145.93%	-29.95%	108.23%

Source: Unconsolidated reports, Bloomberg
Calculations: ELANA Trading

The comparative valuation method showed that shares of First Investment Bank are undervalued. The fair values of shares are very similar when considering equity and profits. The bank is traded at a very low price-to-asset ratio, which suggests that it is undervalued based on market share and position in the local banking sector. To summarize, the fair price of FIB is two times higher than the current price, without an imbalance between the target prices according to P/B and P/E.

Table 2, Forecasts

	2009	2010	2011	2012E	2013E	2014E	2015E	2016E
Total Assets	4 095 287	4 943 973	6 101 669	6 864 378	7 550 815	8 456 913	9 471 743	10 655 711
Loans and Receivables	3 163 298	3 447 076	4 367 699	4 738 953	5 283 933	6 076 523	6 988 001	7 861 502
As Percentage of Assets	77.2%	69.7%	71.6%	69.0%	70.0%	71.9%	73.8%	73.8%
Total Liabilities	3 686 477	4 504 210	5 624 625	6 368 490	7 023 592	7 888 424	8 840 884	9 944 863
As Percentage of Assets	90.0%	91.1%	92.2%	92.8%	93.0%	93.3%	93.3%	93.3%
Total Equity	408 810	439 763	477 044	495 888	527 224	568 489	630 859	710 847
Net Profit	32 019	30 838	36 503	30 890	41 529	54 970	80 510	106 557
Return on Equity	7.83%	7.01%	7.65%	6.23%	7.88%	9.67%	12.76%	14.99%
Return on Assets	0.78%	0.62%	0.60%	0.45%	0.55%	0.65%	0.85%	1.00%

Calculations and estimations: ELANA Trading

The assets growth has decelerated, but not as much as our estimates from last year. This is due to the aggressive policy of the bank for gaining a higher market share, which resulted to decrease in the rate of return. Regarding that trend we are increasing our estimates on the assets and loans growth, whereas the profitability is expected to decrease. Our main assumption is that FIB

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will keep on increasing its assets and maintain a low profit margin. Non-performing loans will have a negative impact on profitability as deepening economic crisis in Bulgaria will postpone the improvement in the credit portfolio. The valuation according to the estimated earnings shows a substantially higher fair price than the current market price. Taking into account a conservative approach to the development of the bank during the next couple of year, we have enough reason to believe that the stock is undervalued.

Discounted cash to equity value:	
NPV five year free cash flow	67 706
NPV terminal value	460 455
Value of shareholders' funds	528 161
Shares issued (thousand)	110 000
Value per share	4.80
Share price	1.36
<i>Premium/(discount)</i>	253.05%

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Recommendation and Price Target

Recommendation: *HOLD*

Target price: **BGN 2.44**

Upside: **79%**

The multiples comparison shows lower fair price compared to the residual income valuation. This inconsistency is increasing due to the lower financial result and the falling multiples of Eastern European banks. We adjust the recommendation to *hold*, as the market is led by the expected issue of shares. We expected for some time that the bank will be forced to raise capital. This should not be taken as bad news in the long run, because it will allow higher profitability as the bank will turn to credits from low-yield Government bonds and cash. However, the market will continue to react negatively as seen in the decrease in share price. However this is a good opportunity for acquiring small packages from the market.

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Financial data

Assets	2008	2009	2010	2011	9M 2012
Cash and cash balances with central banks	587 396	398 874	495 291	772 955	998 848
Financial assets held for trading	9 681	9 023	16 641	8 659	5 909
Financial assets designated at fair value through profit or loss	0	0	0	0	0
Available-for-sale financial assets	286 624	285 110	708 861	644 553	707 191
Loans and receivables	3 103 821	3 163 298	3 447 076	4 367 699	4 682 497
Held-to-maturity investments	60 393	30 018	38 207	54 961	78 656
Derivatives – hedge accounting	274	0	0	0	1 457
Fair value changes of the hedged items in portfolio hedge of interest rate risk	0	0	0	0	0
Tangible assets	149 010	127 683	124 909	115 942	207 864
Intangible assets	5 164	18 115	16 321	14 343	13 602
Investments in subsidiaries	24 920	28 876	34 341	36 371	36 371
Tax assets	2 047	3 270	6 414	4 549	2 864
Other assets	20 796	20 926	22 465	27 224	37 117
Non-current assets and disposal groups classified as held for sale	6 008	10 094	33 447	54 413	0
Total Assets	4 256 134	4 095 287	4 943 973	6 101 669	6 772 376
Deposits from central banks	0	0	0	0	0
Financial liabilities held for trading	0	0	0	0	0
Financial liabilities designated at fair value through profit or loss	0	0	0	0	0
Financial liabilities measured at amortised cost	3 877 460	3 677 884	4 497 390	5 617 141	6 266 296
Financial liabilities associated with transferred financial assets	0	0	0	0	0
Derivatives – hedge accounting	1 336	248	247	358	0
Fair value changes of the hedged items in portfolio hedge of interest rate risk	0	0	0	0	0
Provisions	0	0	0	0	0
Tax liabilities	2 683	2 901	4 051	3 916	3 466
Other liabilities	4 185	5 444	2 522	3 210	3 580
Share capital repayable on demand	0	0	0	0	0
Liabilities included in disposal groups classified as held for sale	0	0	0	0	0
Total Liabilities	3 885 664	3 686 477	4 504 210	5 624 625	6 273 342
Issued capital	110 000	110 000	110 000	110 000	110 000
Share premium	97 000	97 000	97 000	97 000	97 000
Other equity	0	0	0	0	0
Revaluation reserves and other valuation differences	-6 467	-146	-32	746	843
Reserves (including retained earnings)	119 006	169 937	201 957	232 795	269 299
Treasury shares	0	0	0	0	0
Income from current year	50 931	32 019	30 838	36 503	21 892
Interim dividends	0	0	0	0	0
Minority interest	0	0	0	0	0
Total equity	370 470	408 810	439 763	477 044	499 034

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Continuing operations	2008	2009	2010	2011	9M 2012
Financial & operating income and expenses	209 635	192 987	210 802	243 868	177 280
Interest income	333 421	359 724	392 681	432 610	338 354
Interest expenses	189 069	234 823	258 930	276 181	229 918
Expenses on share capital repayable on demand	0	0	0	0	0
Dividend income	69	386	32	438	574
Fee and commission income	69 656	55 993	61 810	78 946	60 430
Fee and commission expenses	9 046	7 174	7 451	8 166	7 154
Realised gains (losses) on financial assets & liabilities not measured at fair value through profit or loss, net	-1 581	600	4 551	-2 192	2 325
Gains (losses) on financial assets and liabilities held for trading, net	-3 773	8 365	7 369	9 596	5 422
Gains (losses) on financial assets and liabilities designated at fair value through profit or loss, net	0	0	0	0	0
Gains (losses) from hedge accounting, net	0	0	0	0	0
Exchange differences, net	5 619	-565	950	1 522	863
Gains (losses) on derecognition of assets other than held for sale, net	0	0	0	0	0
Other operating income	4 710	10 613	10 163	7 561	7 347
Other operating expenses	371	132	373	266	963
Administration costs	139 556	130 267	130 332	147 728	115 288
Depreciation	16 796	17 822	20 522	21 160	15 202
Provisions	0	0	0	0	0
Impairment	-2 742	8 615	25 666	34 370	22 455
Negative goodwill immediately recognised in profit or loss	0	0	0	0	0
Share of the profit or loss of associates and joint ventures accounted for using the equity method	0	0	0	0	0
Profit or loss from non-current assets and disposal groups classified as held for sale not qualifying as discontinued operations	0	0	0	0	0
Total profit or loss before tax from continuing operations	56 025	36 283	34 282	40 610	24 335
Tax expense (income) related to profit or loss from continuing operations	5 094	4 264	3 444	4 107	2 443
Total profit or loss after tax from continuing operations	50 931	32 019	30 838	36 503	21 892
Profit or loss after tax from discontinued operations	0	0	0	0	0
Total profit or loss after tax and discontinued	50 931	32 019	30 838	36 503	21 892
Profit or loss attributable to minority interest	0	0	0	0	0
Profit or loss attributable to equity holders of the parent	50 931	32 019	30 838	36 503	21 892

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For more information, please contact:

Research analyst
Tsvetoslav Tsachev
Tamara Becheva

Phone:
+359 2 810 00 23
+359 2 810 00 27

E-mail:
tsachev@elana.net
becheva@elana.net

Internet:
www.elana.net
www.elana.net