

FIRST INVESTMENT BANK
INDUSTRY: BANKS
GETTING BACK ON TRACK, BUT NOT QUITE

FIBANK, 3RD LARGEST BANK IN BULGARIA IN ASSETS, GRADUALLY RECOVERS FROM THE 2014 FINANCIAL DISTRESS FUELED BY A SIGNIFICANT NET INTEREST INCOME RISE IN LINE WITH THE TREND IN THE SECTOR. NEVERTHELESS, THE BANK COULDN'T FULLY EMULATE THE LATTER DUE TO HIGHER IMPAIRMENT COSTS ON ITS UNSEASONED LOAN PORTFOLIO. MOREOVER, WEAK CORPORATE GOVERNANCE, BORROWER CONCENTRATION AND LOW PROBABILITY OF ADDITIONAL EXTERNAL SUPPORT URGED FITCH TO DOWNGRADE FIBANK'S RATING TO B- FROM BB-.

STRONG BEGINNING OF THE YEAR FOR THE BANKING SECTOR

In Q1 2015, the Bulgarian banking sector realized a 27% y-o-y profit growth, amounting to BGN 285 m, fueled by changes in the pricing strategies and lower impairment expenses. The trend slightly cooled down by May'15 to a profit growth of 22.8% to BGN 447 m and total impairments of BGN 321 m (down 4.6% y-o-y). A third of the profit growth comes from higher taxes and commissions while most of the other part is due to the jump in net interest margin caused by vastly lowering the rates of the deposits. After the fall of Corporate Commercial Bank clients are looking for safer banks to put their money in even if it means earning lower rates. Fibank's reputation of offering some of the best terms would guarantee its clientele.

FIBANK STRAYING FROM THE TREND

Despite the strong quarter for the banking sector, Fibank has not followed suit. Its quarterly net income has fallen by almost 50% y-o-y due to 50% rise in loan provisions and flat fees, which eat out the 21.65% rise in net interest income. The last, however, together with asset growth outperformed our forecasts. Liquid assets increased significantly with cash reaching 19% of assets in Q1'15. Net income from fees and commissions has not reflected the sector's rising trend and has decreased by 0.74% diverting from our 12% y-o-y growth forecast.

SEVERE CREDIT RATING DOWNGRADE, WORKING ON CORPORATE GOVERNANCE

Low probability of additional external support, weak corporate governance and borrower concentration urged Fitch to downgrade Fibank three notches to B- from BB- in its May review of the bank's rating. The outlook is stable. Nevertheless, with the ongoing bank restructuring plan approved by the European Commission and the appointment of a new independent member to the Supervisory board with experience in corporate governance and risk management, Fibank made a decisive step in improving the weaknesses in its system.

VALUATION/RISKS

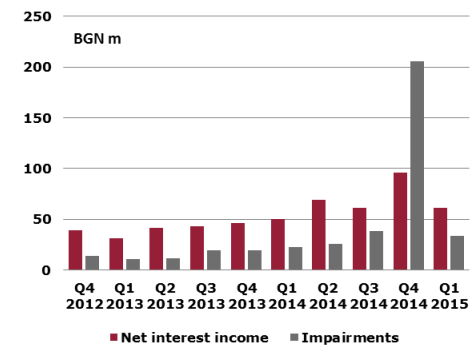
VALUATION: Due to Fibank's underperformance vs the sector we keep our HOLD recommendation but lower our 1YR target price from BGN 3.36 to BGN 2.07 per share as we increase our loan impairment expectations and decrease our asset growth expectations.

RISKS: Expectations that the Fed would raise interest rates to induce less borrowing worldwide; the election of a new governor of the Bulgarian National Bank to lead to restructuring on a local level; local banks asset quality review expected 2016; Possible spillover effects from Greece to affect people's trust in the financial sector.

in k BGN, excl. ratios	2014	2015 (f)	2016(f)	2017(f)
Assets	8,645,835	8,948,439	9,351,119	9,865,431
Equity	728,283	751,226	779,695	811,714
Interest Income	503,731	515,502	490,934	466,763
Operating Income	784,314	646,811	632,528	613,679
Net provisioning for impairment losses	291,827	196,705	182,347	140,770
Operating Expenses	750,345	619,567	598,708	575,752
Net Income	30,455	24,520	30,438	34,134
ROAA	0.38%	0.28%	0.33%	0.36%
ROAE	4.81%	3.31%	3.98%	4.29%
Cost to Income	39.38%	47.89%	49.87%	55.94%
Net Interest Margin	4.26%	4.37%	4.08%	3.46%
Diluted EPS	0.28	0.22	0.28	0.31
P/E	10.11	10.77	8.67	7.73
P/B	6.62	6.83	7.09	7.38

RESULTS ANALYSIS
HOLD
ONE YEAR PRICE TARGET: BGN 2.07
CURRENT PRICE: BGN 2.45
EXCHANGE RATES
EUR/BGN(FIXED): 1.95583
USD/BGN: 1.76309
MARKET DATA

Shares Outstanding:	110m
Share Capital:	110m
Free-float:	15.0%
Market Cap.:	BGN 269.5m
Avg. Daily Vol.:	BGN 29,000
52 Weeks Range:	BGN 2.39-3.40
BSE Ticker	5F4
Bloomberg Ticker	5F4 BU

LOAN IMPAIRMENTS SPEEDING UP


Source: Company data

UNDER PRESSURE SINCE BANK TURMOIL LAST JUNE


Source: Bloomberg

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ANALYST'S COMMENTS

Performance breakdown: in Q1 2015, First Investment Bank (Fibank) reports 21.65% y-o-y increase in net interest income due to lower deposit rates. However, it has not been followed by a proportionate increase in profits due to a 50% surge in impairments on its unseasoned loan portfolio as the bank doubled its balance sheet in the post 2008 crisis period. Fibank's higher impairment costs stray from the general trend in the Bulgarian banking sector of declining loan impairments. Fibank realized strong growth during the peak times of the economic slowdown, when the rest of the banks in Bulgaria were very cautious in their lending activity. The other very aggressively expanding bank in the country – Corporate Commercial Bank, collapsed in June 2014. Its failure led to a bank run in the country with Fibank most affected. This urged the bank to ask for a liquidity support from the state and it received one in the amount of BGN 1.2 bn, approved by the European Commission (EC) in June 2014.

Handling the state deposit well: After receiving government support in 2014, the Fibank has improved its liquidity standing and is now able to perform its business operations as usual. In Q1'15, the bank's assets are up 2.51% y-o-y to BGN 8.9 bn, slightly exceeding our expectations of a 2% asset growth in 2015. The first quarter financial performance reveals the bank's improving health as it is able to repay earlier part of the state support. The state liquidity injection matures on May 28th, 2016 after being prolonged from November 2014. Fibank already repaid 30% of it. In addition, in order to ensure that its creditworthiness is intact, Fibank has increased its cash on hand and liquid buffers to 19% of assets. The bank will also solidify its stability by continuing with its policy to pay no dividends, launch no aggressive commercial activities and undertake no acquisitions as stipulated in the restructuring plan approved by the EC. We expect the bank to regain its pre-2014 crisis deposit base in 2016, excluding the state support, as also stipulated in the restructuring plan.

Profitability and efficiency yet to improve: As already mentioned, higher impairment costs have eaten up the improvement in net interest income. Thus, Fibank's Q1 profitability is below its 5YR normalized earnings. We expect it to remain subdued until 2016, when EPS and ROE should return to normal and increase slightly to an average of BGN 0.38 and 5%, respectively. Nevertheless, with the upcoming bank assets quality review in 2016 announced by the state, Fibank may be encouraged to look for additional earnings pockets from further efficiency improvement as aggressive growth is unavailable due to the restructuring plan. It has already improved its cost-to-income ratio by 10% y-o-y down to 59.66% as of the end of March, 2015. Further improvement below 50% will be a positive surprise. Thus, we decrease our assets growth forecasts from a 5YR average of 5.8% to a 4.4% in the 2015-2019.

Downgraded by Fitch: Room for efficiency improvement seems abundant as Fibank takes notice of the key issue highlighted in May by Fitch when the agency downgraded the bank's credit rating by three notches to B- from BB-. Fitch's key findings include three main issues: (1) low probability of additional sovereign support due to general central banks tightening policies; (2) weak corporate governance and (3) large borrower concentration.

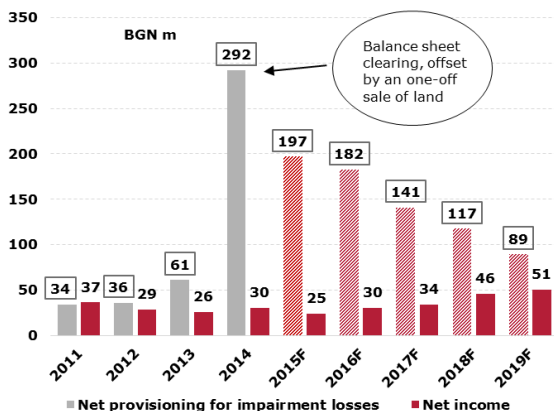
Steps taken by Fibank: To address some of the issues, highlighted by Fitch and stipulated also by the EC in the approved restructuring plan, the bank has already tried to bolster its corporate governance and risk management by hiring a new independent member of the Supervisory board Jyrki Koskelo, with restructuring and corporate governance experience at the IFC. Koskelo acts also as a Monitoring Trustee to the European Commission as prescribed by the restructuring plan.

Additionally, Fibank partnered with the IFC which has made a review of the current corporate governance and risk management policies of the bank as demanded by the restructuring plan. Currently, it is working on implementing the respective recommendations and adopting a full corporate governance code. Also, the bank tries to improve its risk profile by changing its underwriting policies and risk management at the loan origination, which would result in a better choice of clients. The largest credits are to be monitored and forecasted every three months so that it can be certified that they would be able to make their payments. FIB also tries to break the concentration of credits by offering more loans to the retail sector.

In line with our expectations, "Fitch believes that the implementation of the plan could have a moderate positive impact on the risk characteristics of the newly underwritten exposures and lead to somewhat better control over the legacy portfolio. However, given the size of the largest exposures, their long-term nature and limited amortization, risks related to the legacy portfolio will at best unwind only gradually and will weigh on FIBank's risk profile over the medium term", the rating agency said in its Fibank's rating downgrade report. The agency sees limited upside potential for an upgrade in the short to mid-term "given that the potentially positive impact of actions taken within the scope of the restructuring plan will take time to feed through, while legacy issues will continue to weigh on the bank's risk profile". "However, amortization of some of the largest credit exposures, reduced risk concentrations and improved performance could lead to an upgrade", the agency added. Accordingly, we also twitch our loan impairments estimates over the 2015-2019 period by 30%.

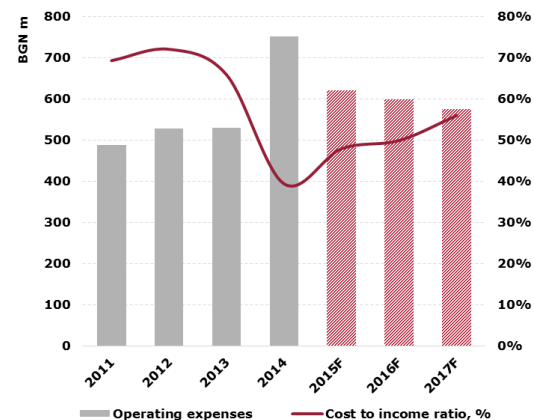
Finally, we expect a supervision tightening at the Bulgarian National Bank with the election of a new governor by October 2015 that would additionally impact the whole banking sector's risk management policies, including Fibank's.

IMPAIRMENTS TO STAY HIGH DUE TO UNSEASONED LOAN PORTFOLIO ACCUMULATED POST 2008



Source: Company data, Elana Trading forecasts

COST-TO-INCOME TO GRAVITATE AROUND 50% TO OPEN UP EFFICIENCY POCKETS



Source: Company data, Elana Trading forecasts

First Investment Bank Overview

Ticker	5F4	Recommendation	HOLD	Outstanding Shares	110 m
Bloomberg ticker	5F4 BU	Last Review	July 10 th , 2015	Free Float	15.00 %
Current Price	BGN 2.45	1Y Target Price	BGN 2.07	Avr. Daily Volume	BGN 29,000

COMPANY PROFILE

First Investment Bank (Fibank) is one of the strongest and most well recognizable bank brands in Bulgaria. It is the third largest bank in the country in terms of assets and the largest listed on the Bulgarian stock exchange. It has one of the biggest branch networks of 168 national branches, 10 in Albania and 1 in Cyprus, and it undertakes financial operations and international payments with over 600 corresponding banks all over the world.

The policies of the bank are very customer-oriented, and it is preferred by both individual and corporate clients, especially in terms of deposits. Fibank commands a 13.5% market share in individual deposits and 8.2% in corporate deposits and is known to offer some of the best deposit terms in the sector. The bank is also a major connoisseur in handling projects sponsored by EU funds, the most famous of which being JEREMIE, a project aimed to provide lucrative credits to SMEs.

FUNDAMENTAL STORY

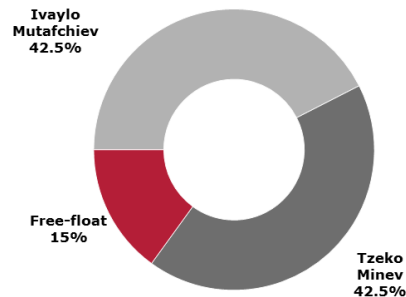
At the present moment, the Bulgarian banking sector is characterized by an environment of carefulness, tightening and strong regulations. The failure of Corporate Commercial Bank (4th largest, Corpbank) last year and the tumultuous situation in the neighboring Greece have sent a signal that the Bulgarian banks would have to be extremely prudent in their operations in order to evade a strong commotion that may have a powerful effect on the economy. Banks have reached extremely high levels of liquidity (30%+ as of May'15) and are constantly cutting their deposit rates in order to make sure that if another crisis occurs, they would be able to handle it.

Fibank has to be most vigilant of all even though it passed the real stress test in June 2014 of the bank run after the fall of Corpbank with a liquidity support from the state approved by the European Commission (EC). Currently, Fibank is working on its efficiency, corporate governance and risk management. The latter should pay-off in the future in terms of higher ROE and even higher customer satisfaction.

STRENGTHS & OPPORTUNITIES

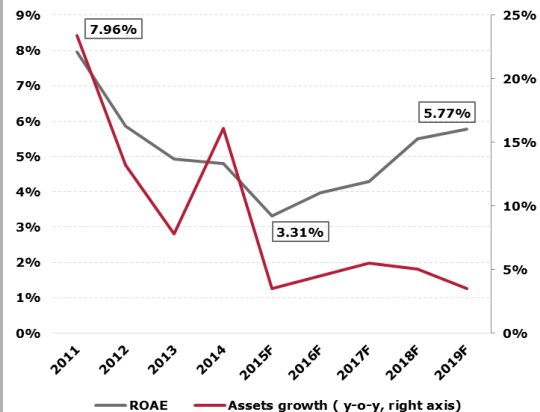
- Viable & flexible bank surviving a real stress test by paying out 13% of assets in a day
- Well recognized bank brand
- High customer satisfaction and loyalty
- Improvement in corporate governance
- Work on more prudent risk management
- Undergoing an EC approved restructuring plan

SHAREHOLDERS' STRUCTURE



Source: Company data

ROAE TO STRENGTHEN AFTER RESTRUCTURING



Source: Company data, Elana Trading forecasts

WEAKNESSES & THREATS

- Higher borrow concentration as stipulated by Fitch in downgrading the bank to B- from BB-.
- Low probability of additional extraordinary state liquidity support
- Turbulence in Greece may have an effect on Bulgarian banking sector

QUARTERLY FINANCIAL DATA

STATEMENT OF INCOME (IN '000 BGN)	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2014	Q4 2014	Q1 2015
NET INTEREST INCOME	39,043	31,193	41,707	42,985	46,449	50,137	68,887	61,181	96,064	60,992
INTEREST INCOME	116,625	105,405	111,672	112,127	117,247	119,778	134,318	126,064	123,571	118,655
INTEREST EXPENSE	77,582	74,212	69,965	69,142	70,798	69,641	65,431	64,883	27,507	57,663
NET COMMISSIONS AND FEES INCOME	18,926	23,255	22,728	19,778	19,676	17,752	23,825	23,263	16,597	17,620
FEE AND COMMISSION INCOME	21,160	25,674	25,430	22,530	22,386	20,695	27,374	26,938	25,851	22,426
FEE AND COMMISSION EXPENSES	2,234	2,419	2,702	2,752	2,710	2,943	3,549	3,675	9,254	4,806
NET TRADING INCOME	1,111	1,775	2,002	1,913	1,917	4,320	2,947	2,881	2,468	3,325
NET FINANCIAL ASSETS INCOME	488	567	1,102	286	374	3,549	4,744	3,103	2,664	3,205
NET OTHER OPERATING INCOME	6,000	1,234	896	638	1,273	1,773	4,616	2,394	143,402	1,989
NET REVENUE	65,568	58,024	68,435	65,600	69,689	77,531	105,019	92,822	261,195	87,131
NET PROVISIONING FOR IMPAIRMENT LOSSES	13,580	10,547	11,548	19,471	19,487	22,400	25,223	38,275	205,929	33,500
NET REVENUE AFTER PROVISIONS	51,988	47,477	56,887	46,129	50,202	55,131	79,796	54,547	55,266	53,631
NON-INTEREST EXPENSE	51,852	51,852	51,852	51,852	51,852	51,852	51,852	51,852	51,852	51,989
ADMINISTRATION COSTS	39,913	34,803	35,758	38,879	44,695	47,313	53,549	48,451	43,356	47,624
DEPRECIATION	5,078	5,012	4,819	4,720	4,569	4,539	4,837	4,790	4,800	4,365
NET OPERATING INCOME	51,988	-4,375	56,887	46,129	50,202	3,279	79,796	54,547	55,266	1,642
NET NON-OPERATING LOSSES (GAINS)	802	155	201	259	310	-73	157	231	3	10
PRETAX INCOME	7,803	7,817	16,956	2,847	1,250	3,206	21,568	2,082	7,113	1,652
INCOME TAX EXPENSES	780	785	1,658	385	177	287	2,181	218	828	180
NET INCOME	7,023	7,032	15,298	2,462	1,073	2,919	19,387	1,864	6,285	1,472
EARNINGS PER SHARE IN BGN	0.26	0.06	0.20	0.23	0.24	0.03	0.20	0.22	0.28	0.01

BALANCE SHEET (IN '000 BGN)	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2014	Q4 2014	Q1 2015
CASH AND CASH BALANCES WITH CENTRAL BANKS	1,025,499	1,350,231	1,122,877	1,102,969	835,926	1,072,871	1,551,970	876,382	983,407	1,657,115
SHORT-TERM INVESTMENTS	717,162	443,122	320,052	378,471	367,769	442,606	303,096	380,764	458,191	610,064
LONG-TERM INVESTMENTS	4,706,451	4,764,652	4,934,307	5,044,064	5,614,671	6,503,422	6,251,410	6,414,328	6,526,190	5,937,674
LOANS AND RECEIVABLES (INCLUDING FINANCE LEASES)	4,577,729	4,644,989	4,766,227	4,837,193	5,390,138	6,284,119	6,161,404	6,349,069	6,460,567	5,821,417
HELD-TO-MATURITY INVESTMENTS	92,351	83,292	131,709	170,500	141,222	182,932	53,635	28,888	29,252	79,886
INVESTMENTS IN ASSOCIATES, SUBSIDIARIES AND JOINT VENTURES	36,371	36,371	36,371	36,371	83,311	36,371	36,371	36,371	36,371	36,371
TANGIBLE ASSETS	401,118	412,893	524,538	540,578	559,195	588,561	641,297	646,268	622,198	640,658
OTHER ASSETS	57,107	57,384	68,582	68,342	68,382	100,877	90,572	84,065	55,849	81,772
TOTAL ASSETS	6,907,337	7,028,282	6,970,356	7,134,424	7,445,943	8,708,337	8,838,345	8,401,807	8,645,835	8,927,283
DEPOSITS FROM CENTRAL BANKS	0	0	0	0	0	0	0	0	0	0
SHORT-TERM LIABILITIES	0	0	0	0	0	0	0	0	0	0
FINANCIAL LIABILITIES MEASURED AT AMORTISED	6,386,247	6,498,025	6,424,547	6,584,567	6,894,990	7,990,844	8,094,093	7,654,993	7,896,088	8,167,466
OTHER LIABILITIES	9,859	11,824	12,372	14,080	12,343	18,886	26,482	27,135	21,464	23,328
TOTAL LIABILITIES	6,396,106	6,509,849	6,436,919	6,598,647	6,907,333	8,009,740	8,120,575	7,682,128	7,917,552	8,190,794
ISSUED CAPITAL	110,000	110,000	110,000	110,000	110,000	110,000	110,000	110,000	110,000	110,000
SHARE PREMIUM	97,000	97,000	97,000	97,000	97,000	97,000	97,000	97,000	97,000	97,000
REVALUATION RESERVES AND OTHER VALUATION DIFFERENCES ON	6,018	6,188	5,893	5,771	7,532	9,194	8,979	9,025	11,343	18,002
RESERVES (INCLUDING RETAINED EARNINGS) & OTHER EQUITY	269,298	298,213	298,214	298,214	298,213	479,484	479,485	479,484	479,485	510,015
INCOME FROM CURRENT YEAR	28,915	7,032	22,330	24,792	25,865	2,919	22,306	24,170	30,455	1,472
TOTAL EQUITY	511,231	518,433	533,437	535,777	538,610	698,597	717,770	719,679	728,283	736,489
TOTAL LIABILITIES & EQUITY	6,907,337	7,028,282	6,970,356	7,134,424	7,445,943	8,708,337	8,838,345	8,401,807	8,645,835	8,927,283

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SELL	Target price is more than 10% below the current quotes

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