

Banca Transilvania Note ahead of Q3'16 results – value (short term) -> growth (medium-to-long term)

TLV RO - Short Note

Q3'16E Results

BUY

previous: BUY

TARGET PRICE 12M (RON)	2.63
Previous Target price	2.76
SHARE PRICE (RON)	2.31

Performance	1M	3M	12M	YTD
Absolute (%)	-3.8%	1.3%	-6.7%	-4.9%
Relative to BET (%)	-2.1%	-0.2%	-2.1%	-2.4%
Market Cap (RON m)			8,422.35	
Market Cap (EUR m)			1,889.27	
Shares Out (m)			3,646.04	

Ahead of Q3 results we still keep a positive view for the stock, despite during last quarter lower end, the stock has posed some increased volatility, major impact coming from the regulatory side – i.e debt discharge and CHF loan conversion law – the latter has no impact for the end of this year, first short term immediate impact being in Q1'17.

Q3 estimates: We believe the third quarter would produce quite robust financials, with bottom line at around 180m, triggered by NIM of slightly above 310 bps, net fees and commissions slightly in range with the last quarters, estimated for Q3 at RON 121m. We see net cost of risk at RON 100m, as we believe the debt discharge difference estimated at RON 250m for the entire year and 174m booked in Q2'16, will be quite equally absorbed via H2'16; which could send Q3'16 bottom line at RON 173m. No reversals from VBRO are expected by year-end. Lending growth rate for mortgages slowed down for Q3 vs. Q2, but is still decent.

Short-to-medium and long term outlook; key risks: For the short term, and excluding potential for a more positive surprise from Q3 results we believe the stock will be played short, or at least volatility will be easily reckoned. For the medium-to-long term, the high M&A potential, although yet no news upon, apart from management known intentions not to pay over book, as well as resilience on sustained growth rates above sector increase would support its growth story potential, and we believe a buy-and-hold strategy would be more suitable. We also believe that after the settle of major impact from CHF and debt discharge law (if any other), less volatility for the stock would be in place. Growth vs. risk will play a much more important role for investors, deeming rather some reserved attitude from Q2'17. Potential for short-to-medium term selling pressure remains.

Due to its high liquidity and capitalization rates, growth estimated to be delivered both organically as well as potentially through new acquisitions, we believe the stock should remain a market outperformer in the medium to long term, but not ahead of Q2'17. Recently, M&A activity witnessed a significant slowdown of 50% Y/Y, reaching some USD 1.1 bn locally, which gives some less upside for the stock from this point of view.

On the other hand, the operating environment seems to be affected mostly by regulatory issues – i.e., the newly enforced debt discharge and more than half way for promulgation by President, and CHF loan conversion law - elections could delay further, with first short-term immediate impact in Q1'17. Another risk is represented by the so much debated law of personal bankruptcy, a very complicated law from legislative point of view, which was send back to the Parliament by the President urging for further clarifications as it does not provide with the required framework to be applied. We view the impact from this law as very late in the future. No impact from AQR next year.

A written and transparent dividend policy could be expected by year-end, but its outcome and release timing could highly depend on current year major KPIs result, as well as management approach toward CHF loan conversion law. This could stop the rather negative stock trend for the year-end.

We keep Banca Transilvania at BUY, with a TP of RON 2.63, with upside at 14%, due to its good financial standing, well capitalized balance sheet and robust key metrics revealed in the past quarters; NIM should stay comfortable slightly above 310 bps, with NPL ratio already at 9%, below sector avg. of 11.3% as of June 2016. Risk balanced portfolio FX mix, with loan book at 70% in RON and equal weight between households and companies. Due to high equity available, as well as limited growth on lending market and large liquidity, we assume a dividend starting FY'17 at some 45% pay-out, which would send FY'17E normalized ROE at some 12%, loosely in line with last 4y average, in our calculations. Long term target is 14%.

31 October 2016

Analyst: Ana Maria Andrus
 ana.andrus@iebatrust.ro

Relatively wise: At TP and currently, the stock trades at a 1.6x (1.7x) P/BV(16E) and 1.5x (1.6x) P/BV(17E), at premium above peers, but we do not believe a relative valuation to be relevant due to its business model advance and growth rates implied. The recent volatility of the stock lowered existing premiums, but not enough to show some discounts. The stock should return to a level of RON 2/share, to mitigate premium at least on P/E, as for P/BV only some large dividend would alter current upside. We believe that in the short term, fundamentals do not allow for such return, unless Q3 results will come with a major negative surprise, which we see less likely. Major reason for TLV at premium over peers is its extra liquidity captured via equity and profitability which supported a lot as well, the positive evolution of the banking system key metrics.

Both trading&fundamentally wise the stock seems more interesting compared to BRD due to a couple of aspects that seem to compensate sector legislative burden. TLV should release by year-end a written transparent dividend policy, comprising a mix of cash and bonus shares, applicable since FY'17, which we believe will replace for the medium to long term, its usual profit capitalization model, and does not carry the issue of too low gap between ROE and CoE like BRD. BRD also suffers more from negative AQR impact next year, while TLV has zero impact. We are more bearish on BRD vs. TLV, despite lower CHF loan law impact, as the business model needs some restructuring and new strategy to capture a higher ROE to support upside in TP. We have a TP of RON 11.6 for BRD, which shows a limited upside potential for the year, unless some major positive surprise in the quarterly results release – less likely in our view.

For TLV, a high payout for the current year will ease the abnormal high ROE and put some down side pressure for the current premiums above peers implied by relative valuation, which under current conditions we find appropriate. We believe that the current small existing premiums in terms of P/E will gradually lower to par by Q1'17 and force a discount once with first impact of CHF loan law conversion, but the prospects of the sector are not represented by a one-time loss taking.

All in all, we believe that RO banks, normalized for one-offs and M&A impact, should trade at a premium, even if a small one, mostly backed by the good macroeconomic profile of the country and good solvability and capacity for shocks absorption via equity, which supported growth development for mortgages and real estate sector. We believe that the regulatory impact (debt discharge and CHF loan conversion) has been overestimated and overplayed so far, as for the current year, CHF loan conversion law impact is nil. We think that current small premiums in terms of P/E will lower even more in Q1'17, when CHF loan conversion will become effective. We believe that the stock should remain a market outperformer in the medium to long term, following all shocks absorbed via equity, and normalization of operating environment, from legislative point of view.

Q3'16 estimates, IFRS, individual:

(RON m) - IFRS	Q1'16A	QoQ	Y/Y	Q2'16A	QoQ	Y/Y	Q3'16E	QoQ	Y/Y
Interest income	509	-24%	33%	492	-3%	28%	476	-3%	19%
Interest expenses	82	-30%	-37%	62	-24%	-47%	65	4%	-33%
Net interest income	428	-23%	68%	430	1%	60%	411	-4%	35%
Net fee income	117	-12%	16%	126	8%	14%	121	-4%	7%
Trading Income	37	-43%	22%	44	18%	10%	38	-12%	-14%
Release of AVFS gains through P&L	60	n/m	n/m	210	252%	467%	19	-91%	n/m
Other income	-41	-169%	n/m	6	n/m	n/m	-3	n/m	n/m
Core&Non-core Income	599	-28%	9%	816	36%	96%	587	-28%	20%
Amort. and depreciation	18	-52%	33%	18	3%	32%	18	-1%	31%
Opex	253	-59%	17%	263	4%	9%	258	-2%	-1%
Pre-provision profit	328	58%	-1%	535	63%	n/m	311	-42%	37%
Loan loss provisions	60	80%	-58%	266	n/m	136%	101	-62%	-7%
EBT	269	11%	41%	270	0%	n/m	211	-22%	43%
Tax on profit	40	-81%	57%	40	-1%	n/m	38	-5%	56%
Net profit	229	-41%	51%	230	1%	n/m	173	-25%	41%

Source: Banca Transilvania, IEBA TRUST;

RECOMMENDATION SYSTEM

SSIF IEBA TRUST uses a Relative recommendation system. Such system indicates that each stock is rated on a basis of the excess return, measured by the relative value of the target (calculated) price and the current price, over a 12 months period of time.

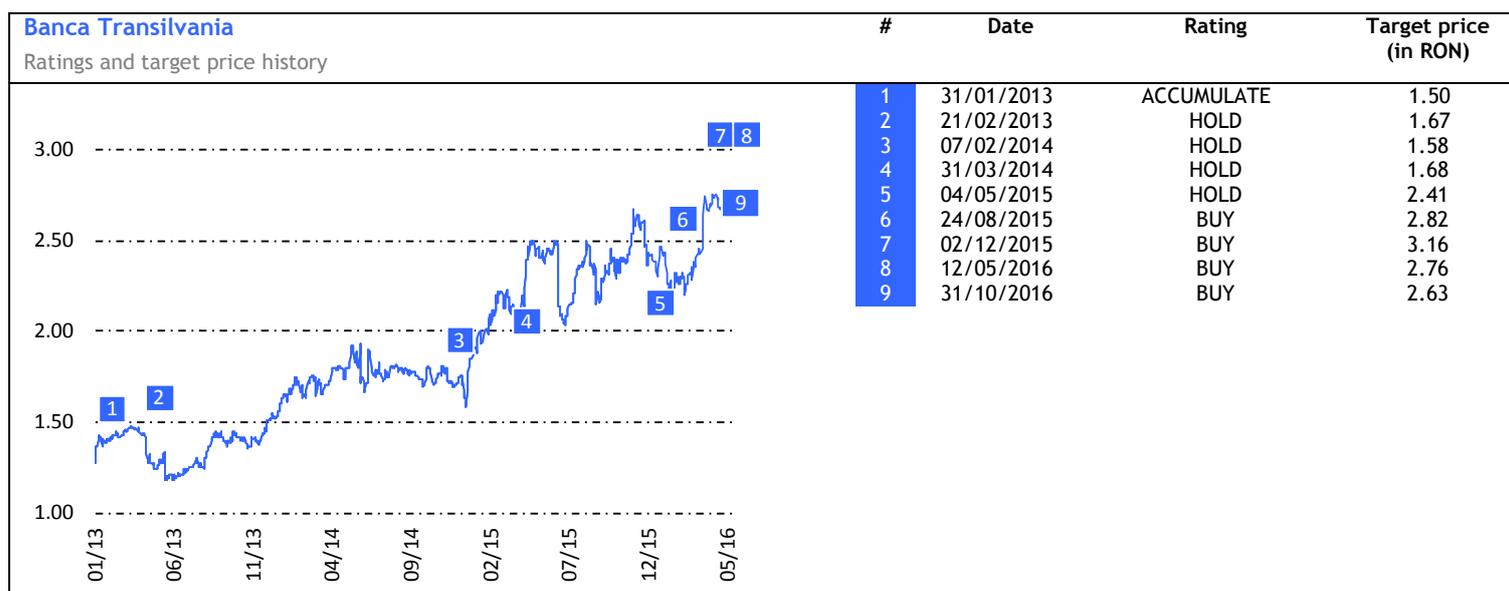
The range of recommendations for each stock consists of 4 elements: Buy (B), Accumulate (A), Hold (H), Reduce (R).

SSIF IEBA TRUST RATINGS

BUY	The stock is expected to generate potential excess return over 15%
ACCUMULATE	The stock is expected to generate potential excess return of 5 to 15%
HOLD	The stock is expected to generate potential excess return of -5% to 5%
REDUCE	The stock is expected to generate potential excess return below -5%

Excess return: Target price/current price - 1

For the cases of Initial Public Offering, the above-mentioned recommendation system is not applied. In such cases, the recommendation is based on the comparison between the price of the Offering, and the fair value estimated by SSIF IEBA TRUST.



Measures Definitions

IEBA Net Income	Adjusted Net Income for one-off items	
Net Cash Flow from operations	EBITDA (+/-) other provisions (+/-)(Increase)/Decrease in Working Capital	
FCF Equity	Net Cash Flow from operations (-) CAPEX	
Net debt	Total short-term and long-term bank debt (-) cash	
EV	Market Cap (avg historic or current) + book value of minorities + Net debt	
FCFPS	FCF Equity	Diluted no of shares
EPS (or IEBA)	Reported (or IEBA) Net Income	Diluted no of shares
BVPS	Total Equity	Year end no of shares
P/E (or IEBA)	Share Price (avg historic or current)	Reported (or IEBA) EPS
P/E IEBA at 52wks High	52 weeks High price (avg historic or current)	IEBA EPS / Diluted IEBA Earnings Per Share
P/BV	Share Price (avg historic or current)	BVPS
ROE	Reported Net Income	Average Total Equity
ROCE	Reported Net Income	Average (Total debt + Total Equity)
EV/EBITDA	EV (with avg historic or current)	Reported EBITDA
EV/EBITDA (x) at 52wks High	EV using 52 weeks High market cap (avg historic or current)	Reported EBITDA
EBITDA/Net financials	Reported EBITDA	Net financials: Net interest (+/-) Net financials
EV/CE (x)	EV (with avg historic or current)	CE: Total bank debt + Total Equity
FCF Yield	FCFPS	Share Price (avg historic or current)
Dividend Yield	DPS	Share Price (avg historic or current)
Dividend Payout	Dividend	Reported Net Income

DISCLAIMER

This report is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in Romania or any other jurisdiction where such distribution, publication, availability or use would be contrary to a law or regulation or which would subject SSIF IEBA TRUST. All material presented in this report, unless specifically indicated otherwise, is under copyright to SSIF IEBA TRUST SA. None of the material, or its content, or any copy of it, may be altered in any way, transmitted to, copied or distributed to any other party, without the express written permission of SSIF IEBA TRUST SA. All trademarks, service marks, and logos used in this report are trademarks or service marks or registered trademarks of SSIF IEBA TRUST SA.

The information, tools, and materials presented in this report are provided to you for information purposes only and are not to be used or considered as an offer, the solicitation of an offer or suggestion to act upon the information presented, nor as grounds for an investment decision. Any other information not included in this material shall be provided to the beneficiary solely upon his request. SSIF IEBA TRUST SA will not treat recipients of this report as its customers by virtue of their receiving this report. The investments and services contained or referred to in this report may not be suitable for you, and it is recommended that you consult an investment advisor or lawyer if you are in doubt about such investments or services. Nothing in this report constitutes investment, service, legal, accounting, or tax advice, or a representation that any investment or strategy is suitable or appropriate to your individual circumstances, or otherwise constitutes a personal recommendation to you. SSIF IEBA TRUST SA does not advise on the tax consequences of investments or services, and you are advised to contact an independent tax adviser. Please note in particular that the bases and levels of taxation may change.

Information and opinions presented in this report have been obtained or derived from sources believed by SSIF IEBA TRUST SA to be reliable, but SSIF IEBA TRUST SA makes no representation as to their accuracy or completeness. The information, opinions and estimations presented in this material reflect the situation at the time of their drafting and can be changed without previous notice. SSIF IEBA TRUST SA accepts no liability for loss arising from the use of the material presented in this report, except that this exclusion of liability does not apply to the extent that such liability arises under specific statutes or regulations applicable to SSIF IEBA TRUST SA. The report was drafted without taking into consideration the financial situation and investment objectives of the beneficiary and is not meant to influence in any and all ways his/her investing decisions. The opinions and proposals presented within the material may be unsuitable to the beneficiary, depending upon the objectives, risk tolerance and financial situation of the beneficiary. This report is not to be relied upon in substitution for the exercise of independent judgment. SSIF IEBA TRUST SA may have issued, or may in the future issue, other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. Those reports reflect the different assumptions, views, and analytical methods of the analysts who prepared them, and SSIF IEBA TRUST SA is under no obligation to ensure that such other reports are brought to the attention of any recipient of this report. SSIF IEBA TRUST SA holds no obligation in updating the material.

SSIF IEBA TRUST SA may, to the extent permitted by law, act upon or use the information or opinions presented herein, or the research or analysis on which they are based, before the material is published. Additional information is, subject to duties of confidentiality, available upon request. Some investments or services referred to in this report will be offered solely by a single entity and in the case of some investments or services, solely by SSIF IEBA TRUST SA or its affiliates. SSIF IEBA TRUST SA may as well participate, invest, effect trades or other operations with the issuers whose securities are the subject of the material.

Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. Certain investments discussed in this report may have a high degree of volatility and may experience sudden and large falls in their value, causing losses when that investment is realized. Income yields from investments may fluctuate as well due to variation of the interest rate, foreign exchange rate, changes in the financials or operational circumstances of the companies and due to other microeconomic or macroeconomic factors. Information, opinions, and estimates contained in this report reflect a judgment at its original date of publication by SSIF IEBA TRUST and are subject to change without notice.

This report may provide the addresses of, or contain hyperlinks to websites. Except to the extent to which the report refers to SSIF IEBA TRUST SA own website material, SSIF IEBA TRUST SA has not reviewed any such site and takes no responsibility for the content contained therein. Such address or hyperlink (including addresses or hyperlinks to SSIF IEBA TRUST's own website material) is provided solely for your convenience and information, and the content of any such website does not in any way form part of this document. Accessing such website or following such link through this report or SSIF IEBA TRUST's website shall be at your own risk.

Important company disclosures

The following designations (a-e) next to a company covered in this publication highlight that one or more members of SSIF IEBA Trust:

- own more than 5% of the share capital of the company (as at the end of the month preceding this publication);
- managed or co-managed a public offering of the securities of the company in the last 12 months;
- has received compensation for financial investment services from the company within the last 12 months;
- is a market maker or stabilizing manager of the company's securities;
- has one or more members in the board of directors or supervisory board of the company

Analyst Certification

The analysts that have written this report certify that the views about the companies and securities contained in this report accurately reflect their personal views and that no part of their compensation was or will be directly or indirectly related to the specific recommendations or views in this report.

RESEARCH

research@iebatrust.ro

Analyst

Ana-Maria Andrus
ana.andrus@iebatrust.ro

SALES & TRADING

Head of Sales

Tudor Cernica
tudor.cernica@iebatrust.ro

Senior Trader

Florin Popescu
florin.popescu@iebatrust.ro

Development Manager

Serban Marin
serban.marin@iebatrust.ro

Head of Corporate

Catalin Nae
catalin.nae@iebatrust.ro

General Manager

George Nistor
george.nistor@iebatrust.ro

SSIF IEBA TRUST

5-7, Dimitrie Pompei Bvd, 5th floor,
Body C, District 2, Bucharest 020335,
Romania

Tel.: +4021 313 0102
Fax: +4021 313 1595