

## Equities

9 February 2012 | 7 pages

# KBC (KBC.BR)

## Alert: 4Q11 Results - Initial Reaction

**Underlying Miss, Reported Beat** – KBC reported net underlying profit of €160m (18% below cons and 25% below Citi). The miss was driven by better than expected pre-provision profit (+17% vs. Citi, +15% vs cons) being more than offset by higher than expected provisions on Greek sovereign debt, the Hungarian mortgage proposals and the Irish loan book. The pre-provision beat was driven by positive marks on FV assets and gains from AFS asset sales. NII was 2% softer vs cons and 3% below our estimates while expenses were 2% better vs. cons and flat vs. Citi. Reported net income at €437 beat our estimate on the back of better CDO marks, MTM of own debt and lower than expected tax rate.

**Belgium Retail Beat** – Belgium net profit of €251m (including €21m post-tax impairment for Greece and €24m impact of the 5-5-5 product) is 28% above consensus driven by higher net realised gains from AFS assets and some comp flex. NII was resilient (+2% qoq and yoy) driven by seasonality, partly offset by weaker NIM (-3% qoq due to the derisking of the government bond portfolio) while volume trends were mixed (mortgage growth up 9% yoy but deposits down 2% qoq, due to the government retail bond, in our view). Costs were down 2% qoq and 7% yoy due to lower variable remuneration and a lower contribution to the Belgian deposit guarantee scheme.

**CEE In-Line** – CEE net profit of €98m was 1% above cons and 5% below Citi estimates. The NPL ratio declined to 5.6%, down 10 bps qoq – in contrast to the Group NPL ratio which ticked up 30 bps qoq to 4.9%.

**Disposals & De-risking (including Sovereign Exposures)** – KBC reduced CDO and ABS exposure by €0.2bn in 4Q11 and by a further €1.7bn in January 2012 (at a “limited cost”). Exposure to Southern Europe sovereign bonds declined 30% qoq to c.€4.4bn. On Kredyt Bank, KBC stated that it is “making considerable progress”.

**Capital & RWAs** - The reported tier 1 ratio declined to 12.3% from 13.6% qoq largely due to RWA impact from Basel 2.5 (€6bn est.) and the €500m repayment of state capital to the Belgian state. The bank now targets to repay €4.7bn of state capital at 15% penalty by the end of 2013. We assume €3bn repayment in 2012 at 15% and €3.5bn in 2013 at 50% penalty.

**Merchant Bank Miss** – MB net loss of -€153m (excluding €26m post-tax impairment for Greece & 5-5-5 product) vs -€60m for cons was driven by higher provisions and weak NII. Commercial banking NII of €147m was down 12% qoq due to a sharp drop in deposits (-€15bn ie down 35% qoq mainly from ‘foreign branches’ in UK, France and Netherlands) and a lower reinvestment yield (from de-risking of GIIPS exposure). Underlying impairments jumped 84% to €379m due to specific provisions on Belgian corporates (from unsustainably low levels) and in Ireland (€228m vs €200m guidance).

**Conference Call 9.30am CET** – Conference call and Webcast will be at 0830 (UK), 0930 (CET). UK dial-in +44 207 1620 177, Belgium +32 2 290 14 11, [www.kbc.com](http://www.kbc.com).

### Company Update

<b>Buy/High Risk</b>	<b>1H</b>
Price (08 Feb 12)	€16.70
Target price	€22.00
Expected share price return	31.8%
Expected dividend yield	4.5%
<b>Expected total return</b>	<b>36.3%</b>
Market Cap	€5,976M
	US\$7,923M

### Price Performance (RIC: KBC.BR, BB: KBC BB)



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## KBC

### Valuation

We have a target price of €22 on KBC. We use a one-stage P/E model to value KBC, including a €4.6bn capital shortfall in our valuation. We also assume 1% growth at a 'normalized' 16% RoTE. We use a cost of equity of 10% based on the company's business mix and the assumption that the capital structure is 'de-risked' via a capital raise. We cross-check this valuation using: (1) comparable price-to-book valuation; and (2) comparable P/E valuation relative to the bank sector. Our target price of €22 equates to 1.0x 2012E BVPS, and 14.9x 2012E underlying earnings (including the coupon payment on the state capital and divestment gains).

### Risks

We rate KBC High Risk because the bank's tangible common equity remains somewhat thin, leaving it highly vulnerable to losses from the regular credit cycle and/or peripheral sovereign debt exposure. However, equally, the very high leverage also allows rapid capital rebuild as we look beyond the current cycle. Through its CEE exposure KBC has emerging market risks of economic disruption, currency devaluation and greater credit risks and has the risk of margin compression and wage/cost inflation as markets mature. These risks could prevent the shares from reaching our target price.

## Appendix A-1

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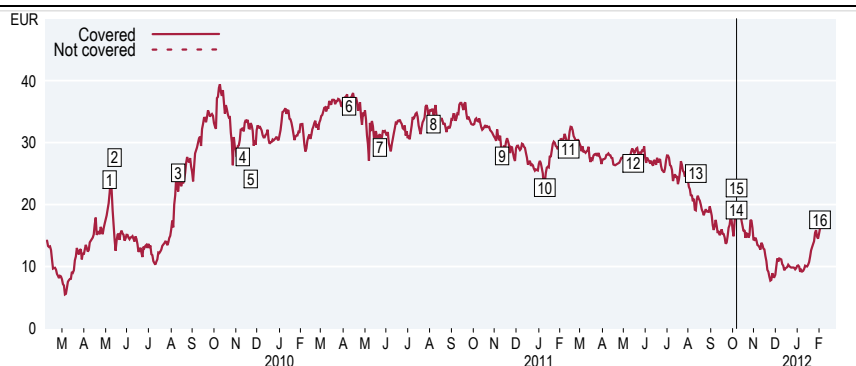
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#### KBC (KBC.BR)

#### Ratings and Target Price History Fundamental Research

Analyst: Stefan Nedialkov

Covered since November 3 2011



Date	Rating	Target Price	Closing Price
1 7-May-09	2H	*24.00	21.90
2 14-May-09	*2S	*15.00	14.34
3 12-Aug-09	2S	*25.00	22.11
4 11-Nov-09	2S	*34.00	32.41
5 23-Nov-09	*2H	*37.50	33.15
6 9-Apr-10	2H	*40.00	36.65

Date	Rating	Target Price	Closing Price
7 24-May-10	*1H	40.00	31.36
8 6-Aug-10	1H	*44.00	34.50
9 11-Nov-10	1H	*41.00	27.85
10 11-Jan-11	1H	*37.00	23.49
11 14-Feb-11	1H	*38.50	30.43
12 16-May-11	1H	*40.00	28.70

Date	Rating	Target Price	Closing Price
13 11-Aug-11	*1S	40.00	19.07
14 7-Oct-11	Stock rating system changed		
15 7-Oct-11	*1H	40.00	18.96
16 2-Feb-12	1H	*22.00	16.15

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

## KBC (KBC.BR)

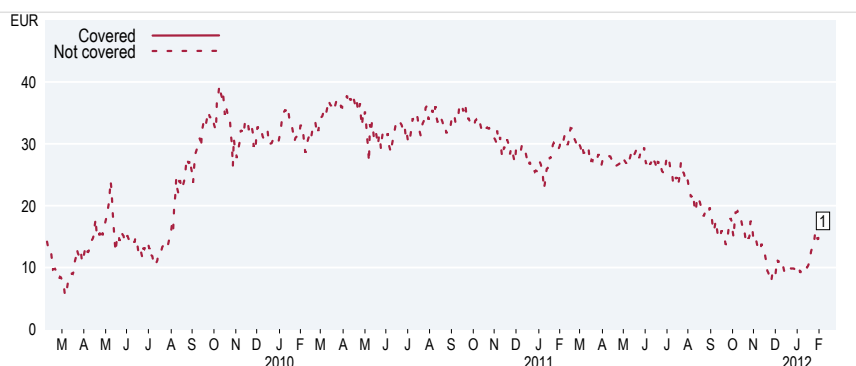
### Ratings and Target Price History

#### Best Ideas Research

#### Relative Call (3 Month)

Analyst: Stefan Nedialkov

Covered since November 3 2011



Date	Rating	Target Price	Closing Price
1 7-Feb-12	*ADD MP	-	17.22

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#### Data current as of 31 Dec 2011

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% of companies in each rating category that are investment banking clients

12 Month Rating			Relative Rating		
Buy	Hold	Sell	Buy	Hold	Sell
57%	34%	9%	10%	79%	10%
45%	41%	40%	49%	43%	41%

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