

Equities

30 September 2011 | 104 pages

Polish Banks

A Difficult Year Ahead

- **Global Turbulence Trumps Solid Results** — Recent financial results have been solid and we expect a strong 3Q but this is likely to be overshadowed by global turbulence.
- **Macro Drives Earnings Downgrade** — On Wednesday, following cuts for the Euro Area (EA), CIRA economists reduced their forecast for Polish GDP in 2012 to 1.9% from 2.9%. This prompts us to reduce our NIM and lending assumptions and lift our NPL estimates. These changes have culminated in an aggregate downward revision to our 2012 net profit estimates for the eight Polish banks under coverage of 23%.
- **Look Also on the Brighter Side of Life** — Balancing the negative flow of forecast downgrades, we note that: (1) in contrast to WE, shareholders of Polish banks, due to lack of material exposure to EA sovereign debt, are less exposed to dilution risk; (2) The impact of a potential Greek default should be mitigated by the fact that it isn't totally unexpected, while (3) the impact of UEFA 2012 on the Polish economy and (4) the EU 2014-20 budget may surprise on the upside.
- **Prefer Defensive Attributes** — Hence we don't advise totally avoiding equity investments but we prefer well capitalized but cost effective, strong fee generating banks with access to relatively cheap and stable retail funding. We also prefer those banks that are less exposed to CHF-denominated mortgage loans and those that are strong in corporate banking, which has strong long-term growth prospects, in our view.
- **Top Pick: Pekao** — Pekao (Buy/Low Risk, TP 171) remains our Top Pick among Polish banks and replaces PZU as our preferred pick among all Polish financials (we still rate PZU Buy/Low Risk, TP 449, but we see a risk that its outperformance of banks will not be sustained). We continue to appreciate Pekao's defensive features which include a high Tier 1, low loan-to-deposit ratio, and limited CHF-lending.
- **BRE and PKO BP for More Bullish Investors** — For less pessimistic investors we recommend BRE (upgraded to Buy/Medium Risk from Hold/Medium Risk, TP ZI 298) and PKO BP (Buy/Low Risk, TP ZI 41) as we think higher exposure to CHF lending and the risk associated with these banks' more aggressive growth strategies of the past are offset by solid capital positions and strong distribution networks: for BRE via mBank (Poland's strongest on-line banking franchise) and for PKO BP via brick-and-click.

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Ticker	Rating		Target Price		Current Year Earnings Estimates		Next Year Earnings Estimates	
	Old	New	Old	New	Old	New	Old	New
BAPE.WA	1L	1L	ZL190.00	ZL171.00	ZL10.52	ZL10.52	ZL11.94	ZL8.94
BGZ.WA	1L	1L	ZL66.80	ZL60.30	ZL2.42	ZL1.61	ZL4.24	ZL1.37
BIGW.WA	3M	3M	ZL5.00	ZL4.53	ZL0.39	ZL0.38	ZL0.47	ZL0.24
BKRE.WA	3M	3M	ZL16.10	ZL12.00	ZL1.26	ZL1.26	ZL1.14	ZL0.34
BREP.WA	2M	1M	ZL318.00	ZL298.00	ZL26.55	ZL26.55	ZL25.19	ZL14.82
BZWB.WA	2M	2M	ZL253.00	ZL239.00	ZL16.72	ZL16.57	ZL18.17	ZL14.67
PKOB.WA	1L	1L	ZL42.90	ZL41.00	ZL3.15	ZL3.14	ZL3.56	ZL3.11
SLAS.WA	1M	1M	ZL930.00	ZL886.00	ZL70.24	ZL68.12	ZL73.16	ZL56.88

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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A Difficult Year Ahead

The global environment is uncertain and has prompted our economists to downgrade their GDP forecasts for Poland. In uncertain times we prefer well capitalised banks due to lower dilution risk and higher dividend potential. We like banks with economies of scale as, according to our analysis, a low cost-to-income ratio and high fee income generation is the only way to achieve above-average return on equity (ROE). We also prefer players with strong franchises both in retail relationship banking, which provides access to stable and relatively cheap funding, and in corporate banking as we see a better growth outlook for corporate lending than in retail lending. We don't expect massive defaults on FX mortgage loans, but due to unpredictable moves on the FX market we highlight associated risks for banks with material exposure to FX loans to unhedged retail clients, i.e. FX mortgages.

We thus prefer Pekao and ING BSK, two banks that enjoy both strong corporate franchises with strong retail franchises, and conservative risk appetite (as proved by the limited exposure to CHF-lending). We also note Pekao's extremely strong capitalization, which makes it a potential active player in M&A, and ING BSK's positive leverage to lower interest rates (due to its exposure to fixed-income instruments in assets and dependence on saving accounts in funding).

Ratings and Ranking

Figure 1. Polish Financials – Trading Multiples

Company	Reuters code	Rating	Target Price	Current price	P/E			P/BV			ROE		
					2010	2011E	2012E	2010	2011E	2012E	2010	2011E	2012E
PZU	PZU.WA	1L	449	317.9	14.3	15.1	10.9	2.1	2.2	2.1	20.3%	17.4%	21.0%
Pekao	BAPE.WA	1L	171	134.0	13.9	12.7	15.0	1.7	1.7	1.7	13.1%	13.3%	11.1%
BGZ	BGZ.WA	1L	60.3	39.8	15.3	24.8	29.0	0.7	0.7	0.7	4.6%	2.7%	2.3%
PKO BP	PKOB.WA	1L	41	32.3	12.5	10.3	10.4	1.9	1.8	1.6	15.4%	17.8%	16.0%
BRE	BREP.WA	1M	298	233.0	13.7	8.8	15.7	1.4	1.2	1.2	11.6%	14.9%	7.7%
ING BSK	SLAS.WA	1M	886	735.0	12.7	10.8	12.9	1.7	1.5	1.4	14.3%	14.7%	11.1%
BZ WBK	BZWB.WA	2M	239	222.0	16.8	13.4	15.1	2.4	2.2	2.1	15.5%	17.5%	14.4%
GPW	GPW.WA	2M	44.5	42.9	19.0	13.6	13.3	3.4	4.7	4.4	18.1%	29.0%	34.0%
Bank Millennium	BIGW.WA	3M	4.53	4.5	15.0	11.8	18.6	1.3	1.2	1.2	9.5%	10.9%	6.6%
Kredyt Bank	BKRE.WA	3M	12	12.3	17.9	9.7	35.6	1.2	1.1	1.1	6.9%	11.6%	3.0%

Prices as of September 29 Source: Powered by dataCentral
dataCentral is CIRA's proprietary database, which includes Citi estimates, data from company reports, and feeds from Reuters, Datastream, Firstcall, IBES and Toyo Keizai

Pekao (Buy/Low Risk, TP ZI 171) remains our Top Pick among Polish banks and replaces PZU (still rated Buy/Low Risk) as our most preferred financial stock in Poland. We like Pekao's defensive features: it enjoys a strong capital position, conservative risk management (e.g. low exposure to CHF lending) and scale, which is crucial in a period of slower growth. Given the bank's high surplus capital, the bank looks to be in a position to benefit from potential M&A opportunities.

Our second pick in Poland is ING BSK (Buy/Medium Risk, TP ZI 886). We appreciate its low exposure to CHF-related loan exposure, its conservative business model, its strong franchise in both corporate and retail banking and the value of its positive leverage to low interest rates.

Taking into account the bank's strong retail franchise, healthy liquidity and capitalisation and limited exposure to CHF lending, and given the statement of the State Treasury and BGK that they have postponed the planned sale of up to 15% of PKO BP's shares in a secondary offering, we rate PKO BP Buy/Low Risk (1L, TP ZI 41.0). We note, however, that due to its appetite for risk PKO BP's earnings in a time of slower economy growth may be negatively affected by higher provisioning.

Our fourth Buy-rated bank is BGZ (Buy/Low Risk, TP ZI 60.3). We like the bank's exposure to defensive industries (agriculture and food production), conservative business model, AAA-ranked strategic shareholder (Rabobank) and attractive valuation, offsetting its low profitability and exposure to CHF loans.

Owing to its strong corporate franchise in Poland and Commerzbank's (its strategic shareholder) franchise in Germany, we think BRE (Buy/Medium Risk, TP ZI 298) is likely to benefit from the strength of economic growth in both countries and an increase in business co-operation. On the other hand, the bank is one of the most exposed to CHF-mortgage lending and despite being hedged against capital and funding stress, it is exposed to rising credit risk as the cost of debt service for its clients is set to increase.

Despite M&A upside risk and inexpensive valuations, we maintain our negative stance on two retail-focused banks given their high exposure to CHF-lending: Bank Millennium (Sell/Medium Risk, TP ZI 4.53) and Kredyt Bank (Sell/Medium Risk, TP ZI 12.0).

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It's All About Europe

Polish GDP Downgraded to 1.9% in 2012

Macro Cuts...

With lower global growth, Greece's non-compliance with the programme conditions and increasing opposition in creditor countries to further bail-outs, Citi economists expect a substantial and probably coercive debt restructuring of the Greek sovereign by the end of 2012 at the latest and likely much sooner (by the spring of 2012 or even December 2011). They expect Ireland and Portugal to follow Greece into sovereign debt restructuring soon afterwards, mainly because of 'political contagion'. With multiple debt restructurings taking place, we expect the euro area to fall back into recession and the ECB to cut rates back to 1.0% by 1Q 2012.

Yesterday, following the material cuts in Euro Area (EA) GDP growth, CIRA economists reduced their forecast for Polish GDP growth in 2012 to 1.9% from 2.9% previously. The main reason for the reduction was expected lower exports, driving lower investments. They expect interest rates to be reduced in 2012 by 50-75bps.

... Lead to Lower Forecast Bank Results

Lower macro forecasts lead us to reduce our estimates of lending growth and to raise our provisioning estimates while the expected drop in interest rates negatively influences our net interest margin (NIM) forecasts. We explain our changes in estimates in more detail in the next section. We note that as our economists expect the Polish economy to rebound in 2013 and grow more than developed Europe, which should lead to increased banking penetration, we maintain our long-term sustainable ROE assumption for the Polish banks.

Figure 2. Polish Banks – Summary of Changes in Net Profit Estimates, 2011E-2013E

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	3,940	3,926	-0.4%	4,446	3,892	-12.5%	4,856	4,005	-17.5%
Pekao	2,761	2,761	0.0%	3,133	2,344	-25.2%	3,552	2,612	-26.5%
BZ WBK	1,229	1,218	-0.9%	1,336	1,079	-19.3%	1,504	1,186	-21.1%
Millennium	476	462	-3.0%	567	292	-48.5%	673	360	-46.5%
Kredyt Bank	343	342	-0.3%	310	94	-69.8%	439	97	-78.0%
ING Bank Slaski	914	886	-3.0%	952	740	-22.3%	1,070	832	-22.2%
BRE	1,117	1,117	0.0%	1,060	624	-41.2%	1,267	667	-47.3%
BGZ	104	69	-33.5%	183	59	-67.7%	262	124	-52.9%
Total	10,780	10,712	-0.6%	11,804	9,064	-23.2%	13,360	9,758	-27.0%

Source: Citi Investment Research and Analysis

Looking on the Brighter Side of Life

Trying to balance the negative flow of forecast downgrades, we highlight four potentially more positive points of view.

Euro Area Perspective: Limited Downside Risk

Despite GDP cuts, CIRA economists believe that the Euro will survive as the Euro Area has the institutional and political capacity to deal eventually with the current crisis and to make the necessary reforms to ensure its long-term survival. Neither elected policymakers nor the ECB have behaved proactively and both are likely to continue to disappoint repeatedly, but our economists believe that ultimately they will find the right solutions. If this is true, the market may be positively surprised (but it also means that the market could fall further before it starts to rise). Banks exposed to defaulting countries may need recapitalization but Polish banks' exposure to Greece, Portugal, Ireland or even Spain and Italy is immaterial. Banks depending on funding from parents are indirectly leveraged to the sovereign debt crisis, but absent uncontrolled bankruptcies of strategic investors (which we do not expect), we see little risk that a sudden withdrawal of funding will trigger a material fall in the value of Polish banks. This makes analysis of potential debt restructuring scenarios largely irrelevant to Polish banks.

Given our base case assumption that there will be no massive banking crisis in Europe, the key issue is the impact of Euro problems on the Polish economy and indirectly on Polish (corporate and retail) clients' demand for funding and ability to pay debts. We will try to address these issues in the coming sections.

What About Greece?

We don't think a Greek default would be as catastrophic as some seem to believe, because it would not come as much of a surprise. It might have noteworthy negative consequences for the European economy, as outlined by our economists, but it would not be a shock event.

UEFA 2012 Euro Upside Risk

In June 2012 Poland and Ukraine will host the UEFA Cup. We sense that the potential positive impact of UEFA 2012 on the Polish economy is not fully taken into account in bottom-up or top-down forecasts for Polish stocks and thus presents a source of upside risk to consensus. The impact may be muted as most of the required investment (in roads, railways and stadiums) was started in previous years. Nevertheless the expected arrival of about 500,000-1,000,000 football fans should positively stimulate consumer demand, and to some extent offset the negative impact of the higher cost of servicing CHF-denominated mortgage loans and the inability of the government to cut taxes as it did during the last crisis. A report commissioned by the Polish government on the impact of preparations for and organisation of UEFA 2012 on the Polish economy estimates tourist spend at ZI c840m in the base scenario. About 5 times higher growth in tourist revenues is expected in 2013-20 due to strengthening the image of Poland as an attractive country for tourism (the so-called "Barcelona effect"). Assuming that each of 500,000 foreign guests spends ZI 1,000 (less than EUR 250) it would mean ZI 0.5bn spending, roughly offsetting the negative impact of a 5% Zloty depreciation on annual instalments on CHF mortgage loans.

European Union 2014-2020 Budget

A draft of the European Union (EU) 2014-2020 budget proposed in June 2012 by EU budget commissioner Janusz Lewandowski faced criticism, mainly from the biggest EU net payers (e.g. the Netherlands and UK) and its final shape is unknown. Nevertheless, it is worth mentioning that the draft proposed an increase in cohesion funds available for Poland to EUR 80bn (more than ZI 320bn) from EUR 67.3bn available in the 2007-2013 budget. Elzbieta Bieńkowska, Polish Minister of the Regional Development expects that, even if the funds are reduced in the final budget vs. the published draft, the amount will be higher than in the current budget.

The development of negotiations on the 2014-2020 budget will be an important driver of changes in economic growth forecasts for Poland in the coming year. The finalization of negotiations is planned at the end of 2012.

We note also that out of EUR 67.3bn funds available in the 2007-2013 budget, as yet only EUR 21bn have been paid by EU; the remainder will be transferred to Poland in the next few years, following project completion and approval. This points to a material change in the budget balance: this year the budget anticipates spending of ZI 60bn on investments and receipt of ZI 40bn from the EU, but next year the net surplus of investments over refunding will be materially reduced and in 2013 the refunding will be much bigger than current investments. We expect this to materially help the government's attempts to reduce the budget deficit in coming years and to improve Poland's image in the eyes of foreign investors.

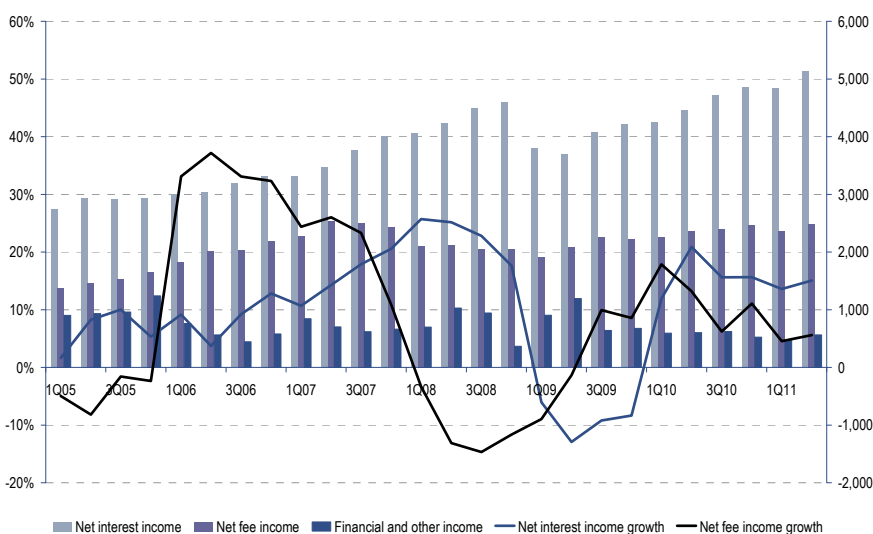
'New Normal' Banking

Looking Back...

2Q11 Take-Aways

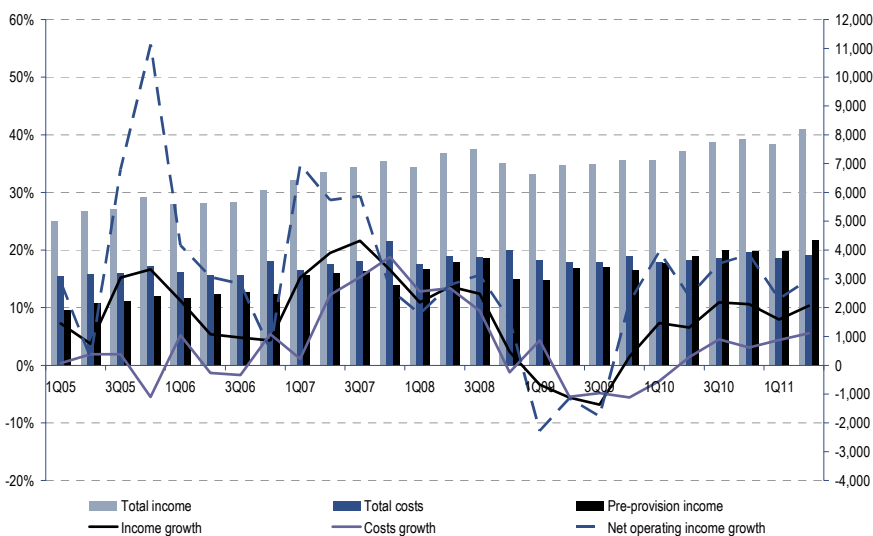
In 2Q11 the net profit of 7 large Polish banks covered by CIRA (we exclude BGZ from our analysis of aggregate data due to its short history of quarterly results) increased by 37% yoy, positively influenced by rising net interest income (+15%) and lower provisioning (-28% yoy) while net fees grew just 6% and administrative costs increased by 6%.

Figure 3. Polish Banks – Revenues of 7 Big Polish Banks, 1Q05-2Q11 (Polish Zloty in million)



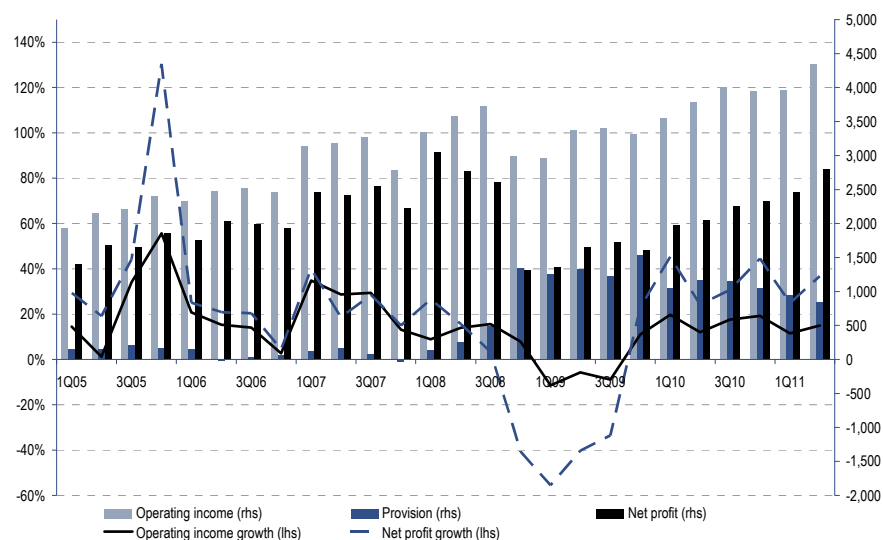
Source: Company reports, Citi Investment Research and Analysis

Figure 4. Polish Banks – Revenues and Costs of 7 Big Polish Banks, 1Q05-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Figure 5. Polish Banks – GOP, Provisioning and Net Profit of 7 Big Polish Banks, 1Q05-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Preview of 3Q11 Results

We will publish our detailed 3Q11 preview in the second half of October but now we present our preliminary general expectations of the trends in Polish banking.

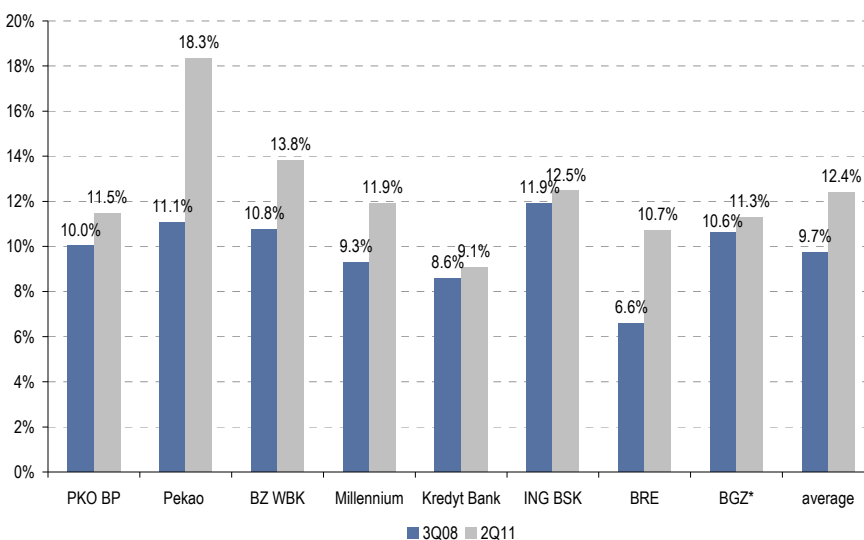
We expect our coverage universe to report solid earnings in 3Q11 as pricing pressure on deposits has remained relatively low while loans have continued to re-price upwards, following average WIBOR, which increased to 4.43% in 2Q11 from 4.10% in 1Q11 (loans used to re-price with a c.3 months delay to market rates). Net provisioning also shouldn't rise materially in 3Q11 as there have been no major bankruptcies while a deterioration in mortgage NPLs has continued in line with trend, without a material acceleration triggered by Zloty depreciation.

Financial Stability Improved

Tier 1 Ratios Higher than in 2008

Due to capital accumulation (dividends from 2008 earnings being paid only by PKO BP, and dividend payments from 2009 and 2010 earnings being lower than before the crisis) and capital increases at PKO BP, Millennium and BRE, the banks' capital ratios are materially stronger than in 3Q08. Pekao and BZ WBK have improved their capital strength the most while Kredyt Bank remains one of the weakest banks in terms of Tier 1.

Figure 6. Polish Banks – Tier 1 Ratios, 3Q08-2Q11 (Percentage)



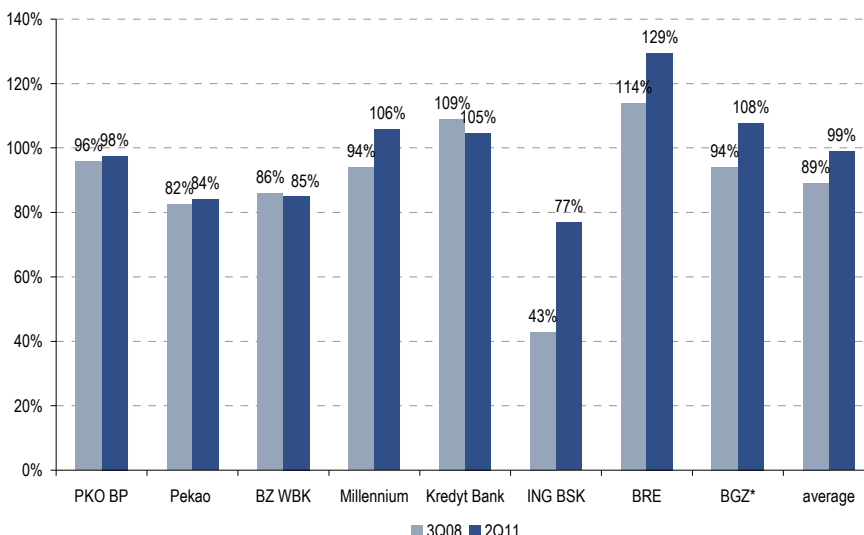
Note: * In BGZ 4Q08

Source: Company reports

High Loan-to-Deposit Ratios Due to Funding From Parents

Compared with 3Q08, loan-to-deposit ratios deteriorated in all covered Polish banks except Kredyt Bank and BZ WBK. In BGZ the increase was caused by a change in funding strategy (replacement of Zloty deposits swapped through CIRS at CHF with medium-term CHF funding from its parent, Rabobank), while in BRE it was due to a change in asset/funding mix (higher in Zloty term value of CHF and EUR mortgages funded directly by parent Commerzbank). We note that the loan-to-deposit ratio adjusted for funding from parents is 86% at BRE and 71% at Kredyt Bank, while the loan-to-deposit ratio adjusted for market stable funding is 101% at Millennium and 92% at PKO BP.

Figure 7. Polish Banks – Loan-to-Deposit Ratios, 3Q08-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

...and Looking Forward

Cutting Net Profit Estimates by 23% in 2012 and 27% in 2013

Lending Growth Estimate Reduced to c8% yoy

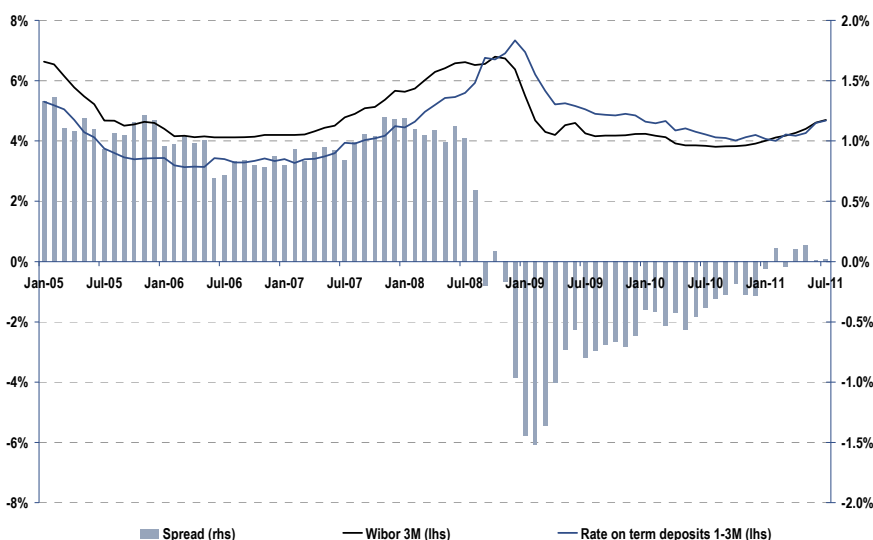
Previously we expected corporate lending to rise c5% yoy in 2012, mortgage loans c12% yoy and consumer loans 5% yoy. This implied sector growth of about 9% yoy in 2012, but we expected our universe of 8 banks, due to better capitalisation and liquidity, to outperform the industry and deliver c11% yoy growth in lending.

Following the revision to our GDP growth forecasts and taking into account current trends, we cut our forecast of growth in retail lending. We expect mortgage loans to rise about 10% yoy and other retail lending to be broadly flat (negatively affected by expected reduction in lending to SMEs). We maintain our forecast of a 5% yoy increase in corporate lending (we note that in July the annual growth rate in corporate lending was +9% so our maintained forecast implies a material deceleration). This implies sector growth of about 6% yoy in 2012. We expect our universe of 8 banks, due to better capitalisation and liquidity, to outperform the industry and deliver c 8% yoy growth in lending.

Net Interest Margin Coming Back to Around 2010 Levels

Rising competition for deposits was started by banks having FX-denominated loans funded by Zloty deposits but the negative impact of a potential “second deposit war” (as it was put by one bank’s IR officer) may be felt by all banks.

Figure 8. Polish Banks – Spread on New Retail Term Deposits, Jan 05 – Jul 11 (Percentage)



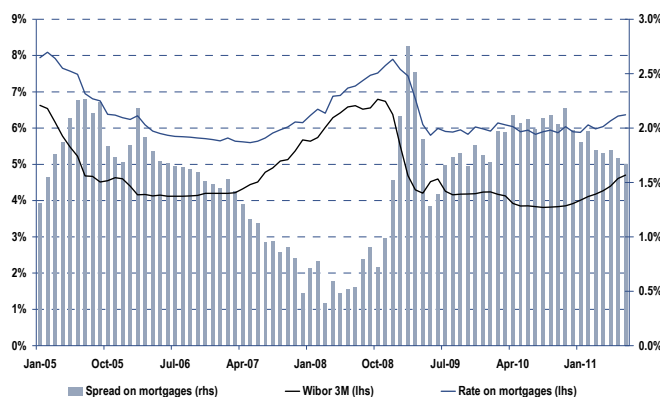
Source: NBP, Citi Investment Research and Analysis

Of CIRA's universe of 8 Polish banks only Bank Millennium and PKO BP fund their CHF-denominated loans with Zloty deposits. Due to PKO BP's diversified funding base (the bank recently issued short term Zloty-denominated bonds, following the issuance of Eurobonds in 2010), strong retail franchise and image among clients as "safe due to state-ownership" we would not expect it to see a major problem with funding even in a negative scenario. Millennium suffered the biggest drop in NIM in 2009 and is potentially exposed to higher-than-industry-average declines again this time; however, we see four reasons why the downward pressure on NIM should be lower than in 2009:

- Firstly, in 2009 the banks were hit by rapid interest rate cuts by the Polish MPC; this time, due to lower starting interest rates, the scope for reduction is much lower; also deposit spreads are much lower than in 2008 (close to zero on new retail term deposits now vs. about 100bp then).
- Secondly, prior to the "deposit war" lending margins were lower than they are now.
- Thirdly, in 2009 the banks suffered not only due to a higher cost of Zloty deposits but also due to increased costs of FX swaps and CIRS; currently the banks have lengthened the maturity of hedging instruments, making them less vulnerable to volatility on the inter-bank market.
- Last but not least, the banks now are better prepared than in 2008 for external shocks; they have contingency plans for liquidity shocks and are able to react in a much more sophisticated manner, rather than just increasing deposit rates across the board. Indeed, in 3Q11 many banks increased the flexibility of relationship managers to increase rates for big deposit clients or tried to access the still active money-market.

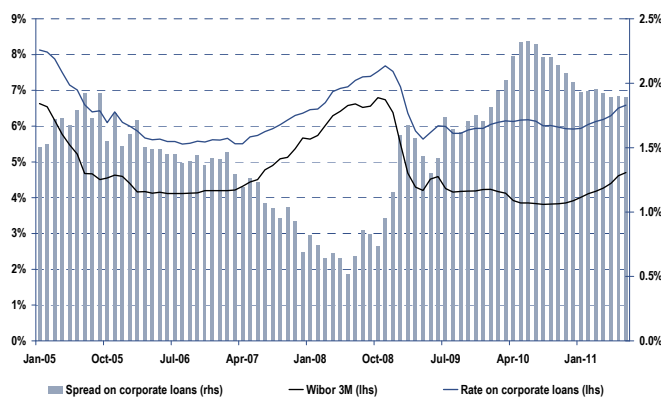
For these reasons we expect NIM to decline only slightly going forward, and be roughly similar in 2012 to 2010 levels.

Figure 9. Polish Banks – Spread on Stock of Mortgage Loans, Jan 05 – Jul 11 (Percentage)



Source: NBP, Citi Investment Research and Analysis

Figure 10. Polish Banks – Spread on Stock of Corporate Loans, Jan 05 – Jul 11 (Percentage)



Source: NBP, Citi Investment Research and Analysis

Figure 11. Polish Banks – Changes in Net Interest Income Estimates, 2011E-2013E (Polish Zloty in million)

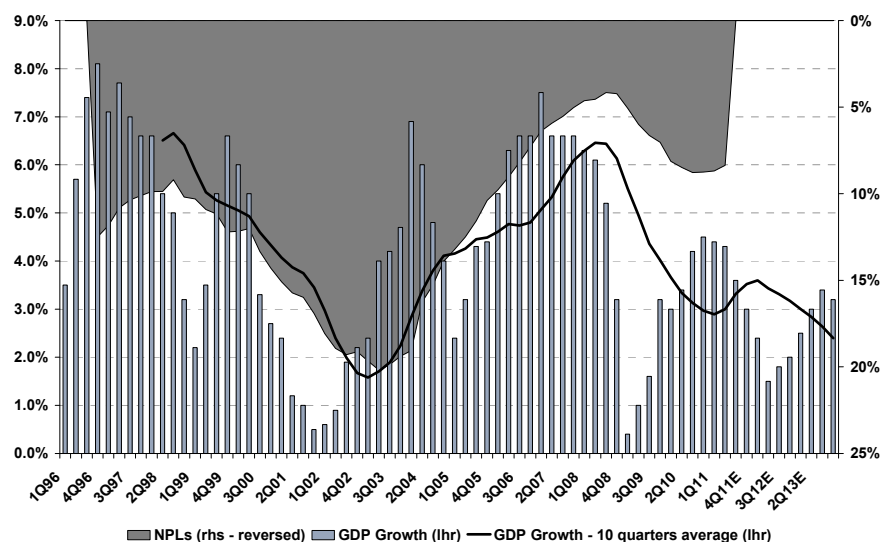
	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	7,384	7,367	-0.2%	7,918	7,784	-1.7%	8,609	8,305	-3.5%
Pekao	4,477	4,477	0.0%	4,947	4,407	-10.9%	5,411	4,694	-13.2%
BZ WBK	2,032	2,018	-0.7%	2,166	2,033	-6.1%	2,376	2,172	-8.6%
Millennium	1,147	1,127	-1.7%	1,292	1,098	-15.0%	1,376	1,171	-14.9%
Kredyt Bank	1,183	1,198	1.3%	1,237	1,174	-5.1%	1,356	1,185	-12.6%
ING Bank Slaski	1,825	1,826	0.0%	1,983	1,937	-2.3%	2,150	2,087	-2.9%
BRE	2,125	2,125	0.0%	2,308	2,019	-12.5%	2,549	2,115	-17.1%
BGZ	794	784	-1.3%	866	803	-7.3%	987	905	-8.2%
Total	20,968	20,922	-0.2%	22,716	21,255	-6.4%	24,813	22,633	-8.8%

Source: Citi Investment Research and Analysis

Our Model Suggests NPLs Will Start Rising in 2Q11

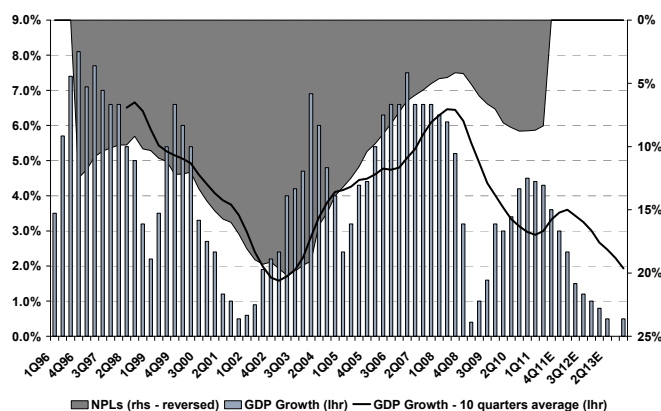
Our simplistic model projecting NPLs on the basis of 10 trailing quarters of yoy GDP growth rates indicates that we should expect NPLs to start rise in 2Q11. It suggests that provisioning will increase as well (vs. our previous assumption of flat provisioning qoq). We expect cost of risk to rise by c50 bps (equivalent to a 1pp increase in mortgage and corporate default loans and a 50% recovery rate; a 75bp increase in consumer lending and a 33% recovery rate). We assume a lower deterioration in asset quality (by just 20bps) at BGZ due to the bank's exposure to mainly defensive food & agricultural sectors and its much better than average performance in terms of asset quality in 2009.

Figure 12. Polish Banks – NPL Ratio vs. GDP Growth (Base Scenario), 1Q95-4Q13E



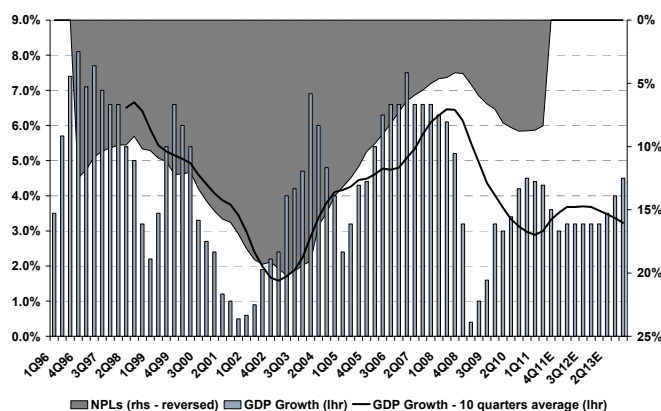
Note: The model is to project timing of changes in NPL ratio trends, not the NPL ratio value.
Source: Company reports, CIRA estimates

Figure 13. Polish Banks – NPL Ratio vs. GDP Growth (Bear Scenario), 1Q95-4Q13E



Note: The model is to project timing of changes in NPL ratio trends, not the NPL ratio value.
Source: Company reports, CIRA estimates

Figure 14. Polish Banks – NPL Ratio vs. GDP Growth (Moderately Bullish Scenario), 1Q95-4Q13E



Note: The model is to project timing of changes in NPL ratio trends, not the NPL ratio value.
Source: Company reports, CIRA estimates

Figure 15. 16. Polish Banks – Changes in Provisioning Estimates, 2011E-2013E (Polish Zloty in million)

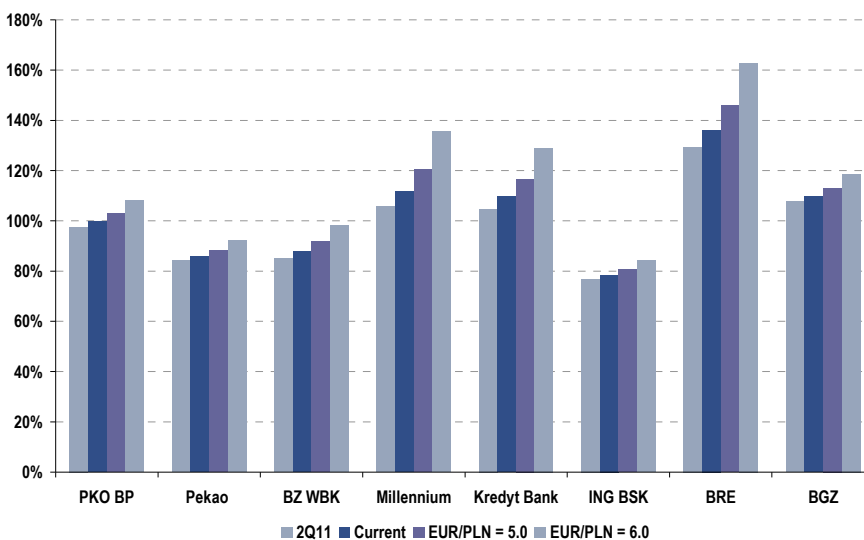
	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	-1,755	-1,755	0.0%	-1,816	-2,365	30.3%	-2,004	-2,757	37.5%
Pekao	-563	-563	0.0%	-639	-1,073	68.1%	-719	-1,162	61.6%
BZ WBK	-348	-348	0.0%	-313	-503	60.5%	-358	-544	52.2%
Millennium	-180	-184	2.0%	-249	-443	77.6%	-245	-475	94.1%
Kredyt Bank	-338	-286	-15.3%	-378	-514	35.9%	-354	-534	50.8%
ING Bank Slaski	-230	-226	-2.1%	-298	-506	69.7%	-332	-559	68.1%
BRE	-423	-423	0.0%	-562	-862	53.3%	-601	-915	52.4%
BGZ	-190	-142	-25.2%	-167	-216	29.0%	-193	-242	25.7%
Total	-4,027	-3,926	-2.5%	-4,423	-6,482	46.6%	-4,805	-7,188	49.6%

Source: Citi Investment Research and Analysis

Capital and Loans-to-Deposit Ratio FX Stress-Tested

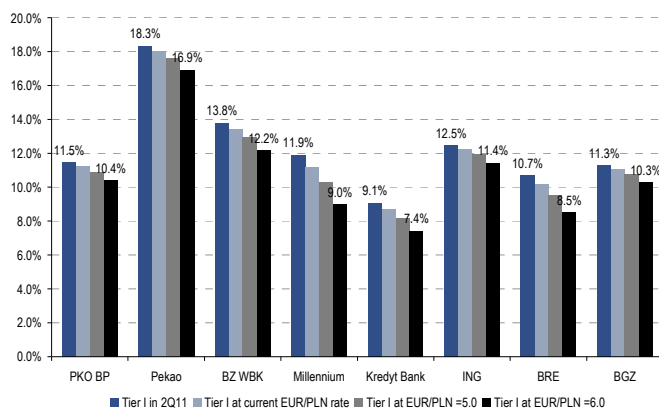
The Zloty continued to weaken against the Swiss Franc in September. In the charts below we show the sensitivity of Polish banks' loan-to-deposit, CAR and Tier 1 ratios to changes in EUR/PLN and CHF/PLN rates (assuming a constant EUR/CHF rate).

Figure 17. Polish Banks – Loan-to-Deposit Ratios Depending on EUR/PLN Rate, 2Q11 (Percentage)



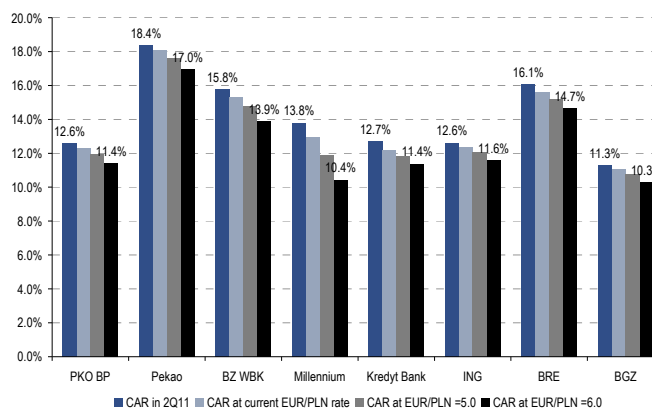
Source: Company reports, Citi Investment Research and Analysis

Figure 18. Polish Banks – Tier 1 Ratio Depending on EUR/PLN Rate, 2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 19. Polish Banks – CAR Depending on EUR/PLN Rate, 2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Credit Risks

FX Loans: Mainly CHF Mortgages and EUR Corporate Loans

Mortgage loans are dominated by CHF mortgage loans and corporate loans by EUR lending. The latter we find relatively safe as such loans used to be granted to exporters with EUR revenues. Of course, lower external demand may cause EUR revenues to decline but rising profitability of the remaining exports should offset some of this impact. The biggest risk we see is in FX mortgage loans.

Figure 20. Polish Banks – FX Structure of Loans, 2010 (Percentage)

	FX	Out of which: CHF	USD	Euro	other FX	Main type of FX loans:
PKO BP *	23%	17%	NA	5%	2%	CHF mortgages and EUR corporate loans
Pekao	23%	9%	2%	12%	0%	EUR corporate loans and ex.BPH (granted before 2007) CHF mortgages
BZ WBK	34%	7%	NA	25%	2%	EUR corporate loans, including CRE loans
Millennium	58%	53%	1%	3%	1%	CHF mortgages
Kredyt Bank	47%	38%	1%	8%	0%	CHF mortgages, some EUR mortgage and corporate loans
ING	22%	5%	1%	16%	0%	EUR corporate loans
BRE	57%	37%	3%	14%	3%	CHF mortgages and EUR mortgage and corporate loans

Source: Company reports, Citi Investment Research and Analysis

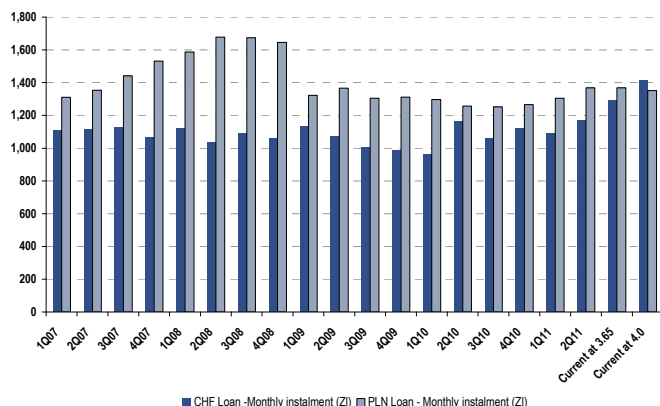
FX Mortgage Credit Risk – Terra Incognita

This Time Is Different

In contrast to 2008-2009, when the material depreciation of Polish Zloty against the Swiss Franc didn't lead to significant deterioration in the asset quality of FX mortgages, this time we expect the high CHF/PLN rate to have a negative impact on the quality of FX mortgages. The biggest difference compared with late 2008/early 2009 is the different performance of CHF LIBOR. As the interest rate on the majority of Polish FX mortgages is linked directly to CHF LIBOR, the drop in CHF LIBOR in 2008 caused a decline in interest rates on CHF-denominated mortgages and offset the depreciation of the Zloty. Thus the overall monthly installment, according to our estimates, remained broadly unchanged.

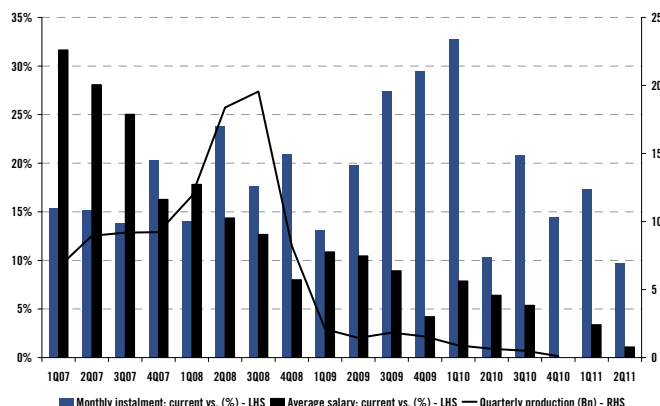
This time, sharp weakening of the PLN versus the CHF was coupled with only a small decline in the CHF LIBOR rate and FX mortgage debtors are paying a monthly installment at least 20% higher than at origination (some clients' installments have even increased about 40%). According to our estimates, only in the case of clients that took out loans before 4Q07 is the increase in monthly installments offset by wage growth. We see no reason to challenge the simple relationship between the sudden increase in the value of monthly payments and the ratio of overdue loans and no reason to expect that the same factor (higher installments) will cause a different result than in Hungary in 2009. Of course, banks may try to help clients cope with the increased burden of debt servicing and temporarily reduce monthly payments and we expect this process to happen, but we do not believe a flexible approach on the part of the banks will be able to fully offset the increased debt service ratio.

Figure 21. Polish Banks – Monthly Installment on CHF 100,000 Mortgage Loan Granted in 1Q07 vs. the Installment at Its Equivalent in PLN, 1Q07-3Q11 (Polish Zloty in million)



Source: NBP, Citi Investment Research and Analysis

Figure 22. Polish Banks – Increase in Monthly Installment on CHF Mortgage Loan Granted in Given Quarters from the Loan Origination, Compared with Increase in Average Salary, 1Q07-2Q11 (Percentage)

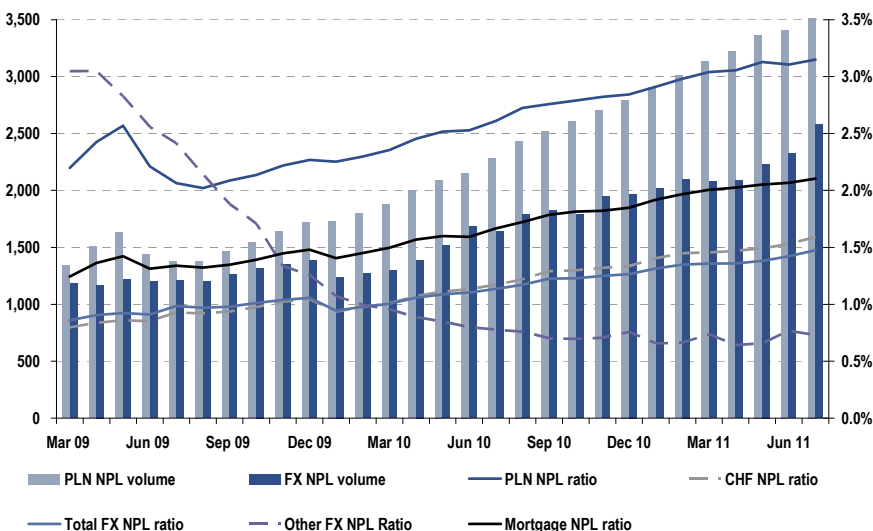


Note: Current instalment calculated at CHF/PLN rate of 3.65
Source: NBP, GUS and Citi Investment Research and Analysis

The increase in monthly installments comes at a moment when asset quality in the mortgage segment continues to deteriorate. The NPL ratio of Zloty-denominated mortgages increased to 3.15% from 3.11% in June and the NPL ratio of CHF-denominated mortgages rose to 1.59% from 1.53% the previous month. Only the NPL ratio of other FX-denominated mortgage loans slightly decreased to 0.73% from 0.77% in June. The total mortgage NPL ratio thus increased to 2.10% from 2.07% in June and 2.05% in May.

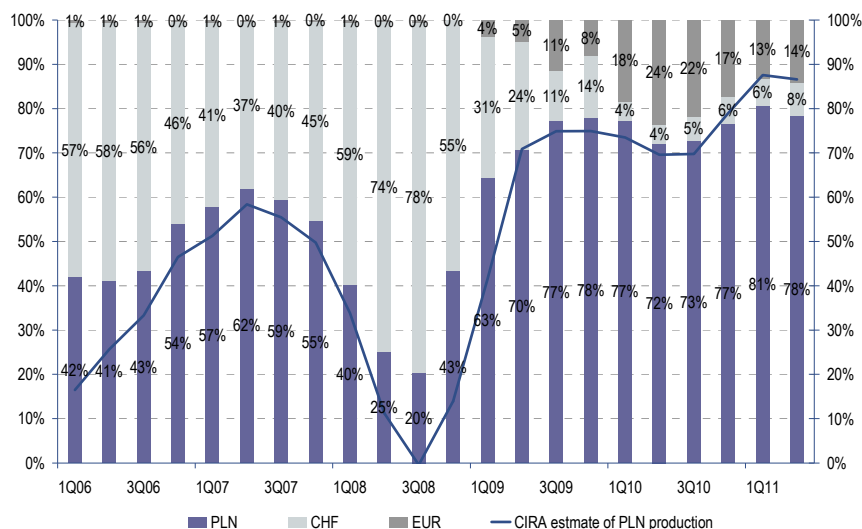
We note that the c3% NPL ratio in non-CHF FX mortgage loans in March 2009 may signal that the natural long-term mortgage NPL ratio in Poland is at that level. Prior to 1Q09 EUR mortgages were not popular and non-CHF mortgages were mainly USD-denominated mortgages granted in the 1990s. Given that they were granted mostly to more affluent clients (mortgage loans became popular after 2002) and real-estate prices were much lower than now, post the 2006-2008 mortgage boom the relatively high NPL ratio is surprising.

Figure 23. Polish Banks – Mortgage NPLs, Mar 09 –Jul 11 (Polish Zloty in million/Percentage)



Source: Company reports, Citi Investment Research and Analysis

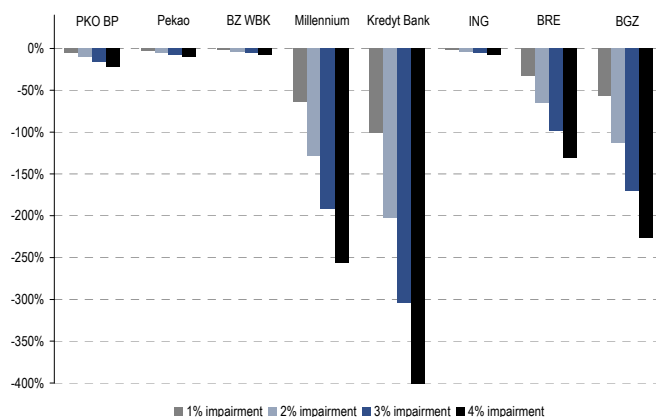
Figure 24. Polish Banks – FX Structure of Mortgage Production, 1Q06-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

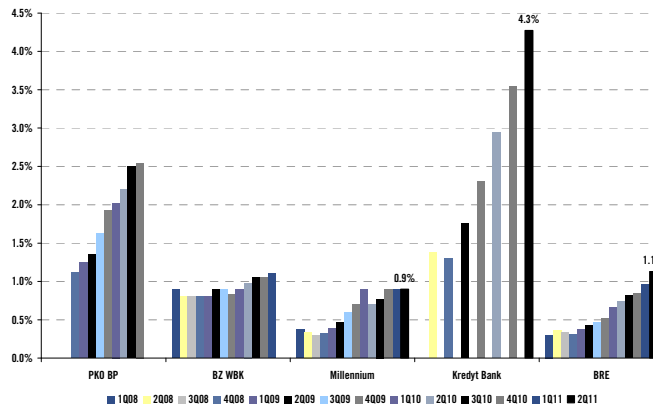
We note that Millennium has the lowest mortgage NPL ratio (0.9%), followed by BRE (1.1%), while PKO BP's (3.0%) and Kredyt Bank's (4.3%) ratios are above the industry average (2.1%).

Figure 25. Polish Banks – Impact of CHF Mortgage Impairment on Net Profit, 2012E (Percentage)



Source: Companies reports, Citi Investment Research and Analysis

Figure 26. Polish Banks – Mortgage NPL Ratios, 1Q08-2Q11 (Percentage)

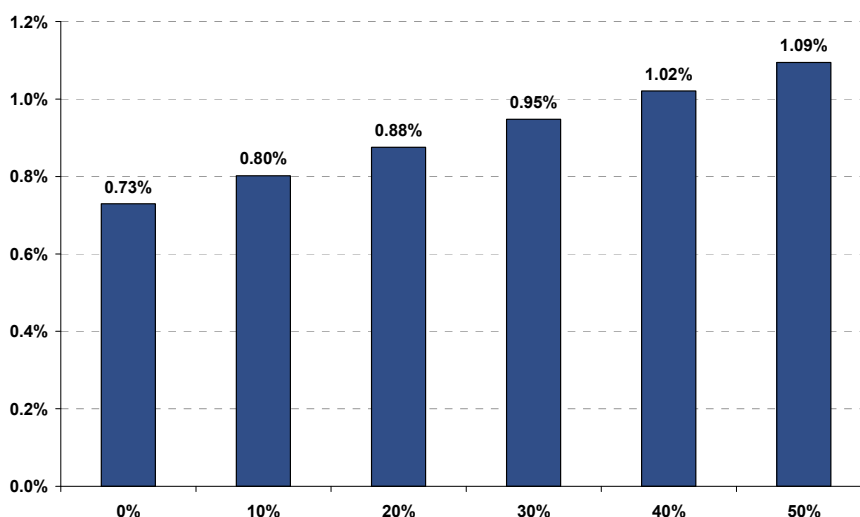


Source: Companies reports, Citi Investment Research and Analysis

Other Credit Risks

The higher cost of servicing FX mortgages by households is a risk factor not only for asset quality of mortgage loans but, indirectly, also for other lending as it may lead to lower consumption and in this way negatively affect the economy. According to our estimates, Zloty depreciation by 10% vs. CHF and EUR leads to a c.1bn increase in the annual cost of servicing FX mortgages. Indeed we estimate that the depreciation of the Zloty by 12% vs. EUR and 14% vs. CHF year-to-date has increased the cost of servicing FX mortgages from c0.73% of GDP to c0.83%.

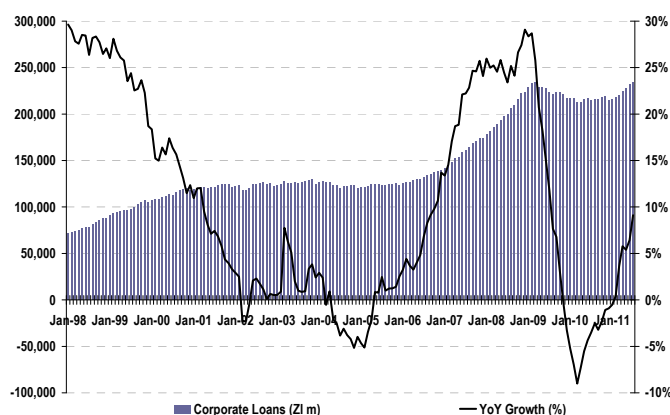
Figure 27. Poland – Aggregated Annual Installment on FX Loans as % of GDP, Depending on Zloty Depreciation YTD, 2011 (Percentage)



Source: CIRA estimates

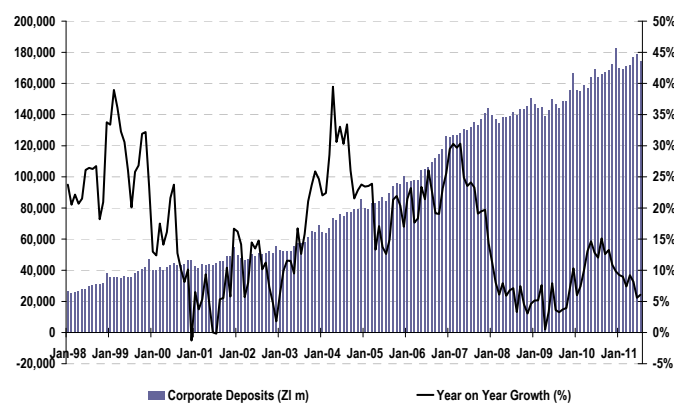
Due to low leverage and high deposits corporates should be relatively resilient to the economic slowdown, but we see a risk that some FX option liabilities swapped into loans in 2009, which should be paid this year, may become the new 'toxic assets' for Polish banks.

Figure 28. Polish Banks – Corporate Loans, Jan 97 – Jul 11 (Polish Zloty in million)



Source: NBP, Citi Investment Research and Analysis

Figure 29. Polish Banks – Corporate Deposits, Jan 97 – Jul 11 (Polish Zloty in million)



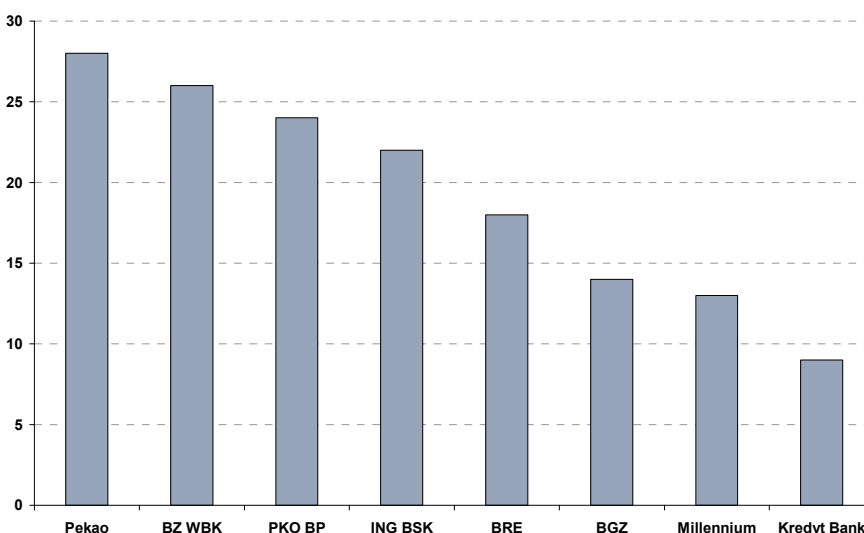
Source: NBP, Citi Investment Research and Analysis

Ideal Bank Attributes in Uncertain Times

Given uncertainty about the prospects of the global economy and turbulent FX rates on the one hand and the opinion of our economists that a global recession will not happen on the other, we prefer defensive stocks. As such, we favour dividend stocks and industry leaders (in the case of the banking industry: banks benefiting from strong retail franchises giving them access to cheap and stable funding). Within Polish banks we prefer banks without material exposure to CHF mortgage loans and with a strong position in corporate banking (as we expect continuation of

the present trend of outperformance of retail lending by corporate lending, in terms of both growth dynamics and asset quality). We prefer banks with low cost-to-income ratio as their profitability is less sensitive to declining revenues. We maintain our general view that only high net fee income will allow banks to achieve above-average ROE. Pekao followed by BZ WBK and PKO BP best match these preferred attributes, based on our analysis.

Figure 30. Polish Banks – Ranking of Business Resistance



Source: Citi Investment Research and Analysis

Figure 31. Polish Banks – Key Measures of Business Resistance

Measure	Capital Tier 1	Cost efficiency C/I Ratio	Fee generation Net fees as % of assets	Retail franchise Current retail accounts as % of total deposits	Corporate know-how Corporate lending (Polish Zloty in million)	Low CHF Risk Share of CHF Loans in total loans
as of	1H11	2010	1H11	2010	2Q11	2010
PKO BP	11.5%	42%	1.8%	22%	31,237	17%
Pekao	18.3%	50%	1.8%	20%	53,053	9%
BZ WBK	13.8%	49%	2.4%	15%	24,222	7%
Millennium	11.9%	63%	1.2%	7%	9,788	53%
Kredyt Bank	9.1%	57%	0.7%	5%	6,988	38%
ING BSK	12.5%	59%	1.5%	11%	19,003	5%
BRE	10.7%	52%	0.9%	20%	24,292	37%
BGZ	11.3%	75%	0.9%	7%	13,786	18%

Source: Citi Investment Research and Analysis

Figure 32. Polish Banks – Ranking of Business Resistance

	Sum	Capital	Cost efficiency	Fee generation	Retail franchise	Corporate know-how	Low CHF Risk
PKO BP	24	3	5	4	5	4	3
Pekao	28	5	4	4	5	5	5
BZ WBK	26	4	4	5	4	4	5
Millennium	13	3	2	3	2	2	1
Kredyt Bank	9	1	3	1	1	1	2
ING BSK	22	4	3	3	4	3	5
BRE	18	2	4	1	5	4	2
BGZ	14	3	1	1	2	3	4

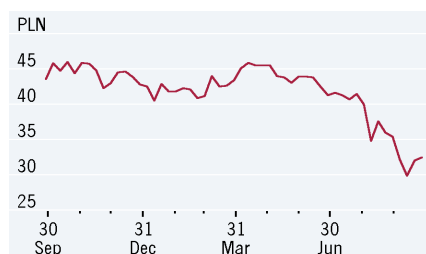
Source: Citi Investment Research and Analysis

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Buy/Low Risk	1L
Price (29 Sep 11)	ZL33.32
Target price	ZL41.00
from ZL42.90	
Expected share price return	23.0%
Expected dividend yield	1.9%
Expected total return	24.9%
Market Cap	ZL41,650M
	US\$12,690M

Price Performance (RIC: PKOB.WA, BB: PKO PW)



PKO BP (PKOB.WA)

Retail Enough to Take a Risk: Maintaining Buy

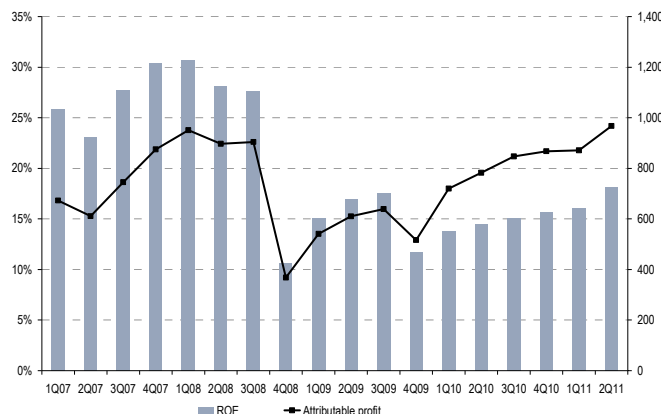
- **Strategy Review** — At their August analyst meeting management summarised progress in reaching goals set in its 2010-12 strategy. Unsurprisingly, it appears that the bank's undemanding financial targets (e.g. >16% ROE) should be met. Our take on the bank's non-financial targets is that management is doing a lot of useful work on improving the bank's internal organisation but is still at the beginning of the road to realisation of its strategic goals. Since the launch of the new strategy, the bank hasn't become more universal and has yet to start branch modernization (crucial for the perception of the bank by clients).
- **High Provisioning Continued** — PKO BP's cost of risk (132bp in 2Q11) is the highest in our universe of eight Polish banks. We used to attribute it to the bank's appetite for risk, manifested by its high share of consumer and SME lending. In 2Q11 we were negatively surprised by the increase in the bank's provisioning on mortgage loans and we see a risk that this trend may even accelerate due to the strength of CHF (CHF mortgages account for 18% of the loan book).
- **Resistant Due to Solid Retail Franchise** — Thanks to the advantage of being the biggest retail bank in the country and the bank of first choice for older and less affluent clients, PKO BP has access to stable funding, is able to generate high fee income and operate with a low cost-to-income ratio. In our opinion, its capital base is solid but not enough to consider a material acquisition (while small acquisitions make little sense for the biggest bank in the country which still needs to modernize its own branches).
- **2012E EPS Cut by 12%** — We reduce our NIM estimate to 4.16% from 4.20% in 2012 and to 4.15% from 4.20 in 2013, lower our loan growth forecasts to 8% from 10% (in both years) and increase our cost of risk to 158bp from 120bp in 2012 and to 170bp from 120bp in 2013. These changes lead us to cut our EPS estimates by 12% and 18% in 2012 and 2013, respectively.
- **Maintaining Buy** — We maintain our assumption of sustainable ROE of 17% but due to lowered 2012 and 2013 EPS estimates we decrease our target price to 41.0 from ZL 42.9 previously. We view the recent share price decline as unjustified and maintain our Buy/Low Risk (1L) rating.

PKO BP (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	2,305.5	3,216.9	3,925.6	3,891.9	4,004.8
Diluted EPS (ZL)	2.07	2.57	3.14	3.11	3.20
Diluted EPS (Old) (ZL)	2.07	2.57	3.15	3.56	3.89
PE (x)	16.1	12.9	10.6	10.7	10.4
P/BV (x)	2.0	2.0	1.8	1.6	1.4
DPS (ZL)	1.90	1.98	0.63	0.62	1.28
Net Div Yield (%)	5.7	5.9	1.9	1.9	3.8
ROE (%)	13.4	15.4	17.8	16.0	14.6

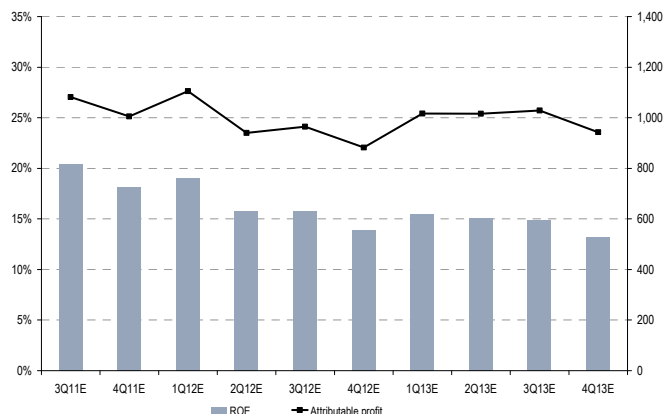
PKO BP in Snapshots

Figure 33. PKO BP – Reported Net Profit and ROE, 1Q07-2Q11 (Polish Zloty in million/Percentage)



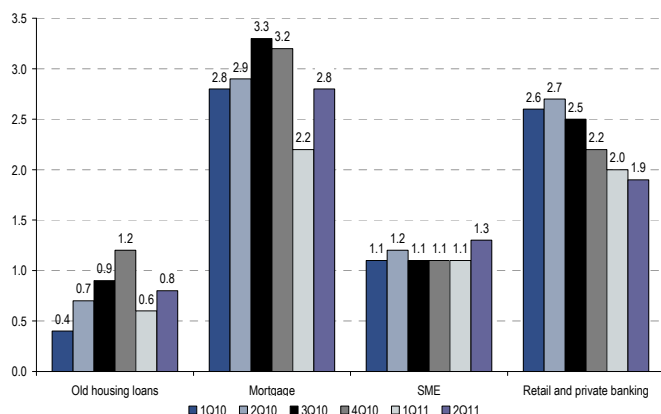
Source: Company reports, Citi Investment Research and Analysis

Figure 34. BPKO BP – Forecast Net Profit and ROE, 3Q11-4Q13E (Polish Zloty in million/Percentage)



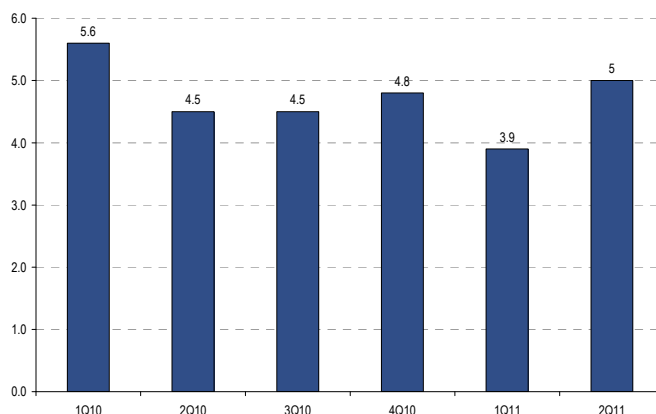
Source: Citi Investment Research and Analysis

Figure 35. PKO BP – Sale of Retail Loans, 1Q10-2Q11 (Polish Zloty in billion)



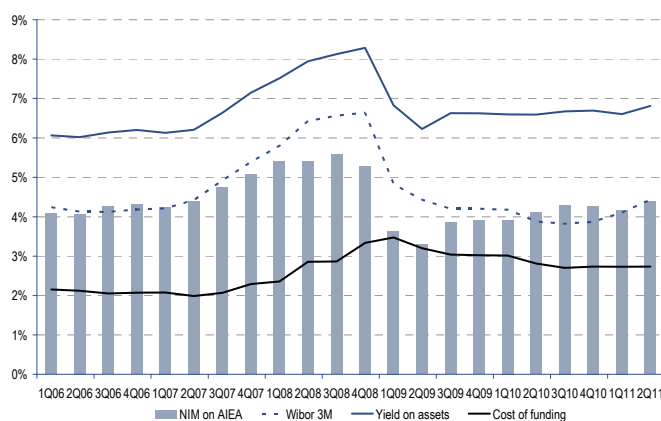
Source: Company reports, Citi Investment Research and Analysis

Figure 36. PKO BP – Sale of Corporate Loans, 1Q10-2Q11 (Polish Zloty in billion)



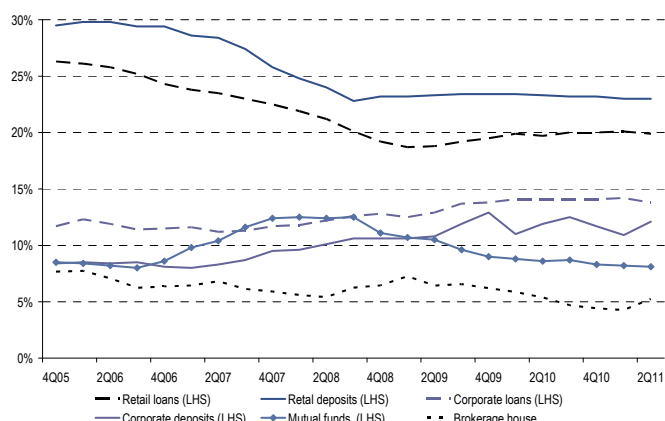
Source: Company reports, Citi Investment Research and Analysis

Figure 37. PKO BP – Yield on Assets and Cost of Funding, 1Q06-2Q11 (Percentage)



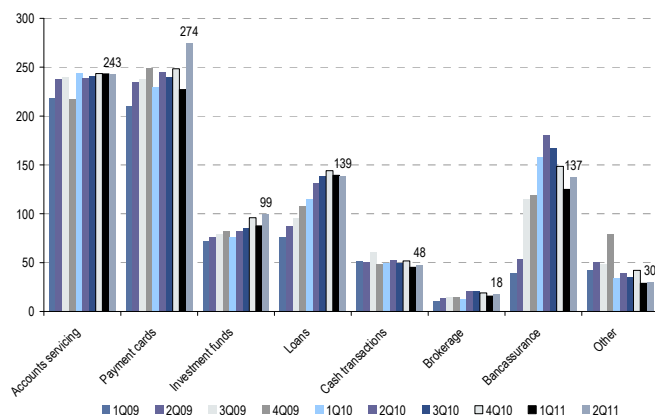
Source: Company reports, Citi Investment Research and Analysis

Figure 38. PKO BP – Market Share, 4Q05-2Q11 (Percentage)



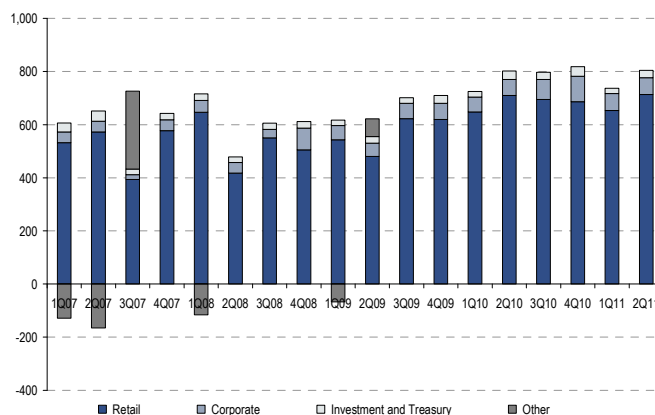
Source: Company reports, Citi Investment Research and Analysis

Figure 39. PKO BP – Breakdown of Net Fees, 1Q09-2Q11 (Polish Zloty in million)



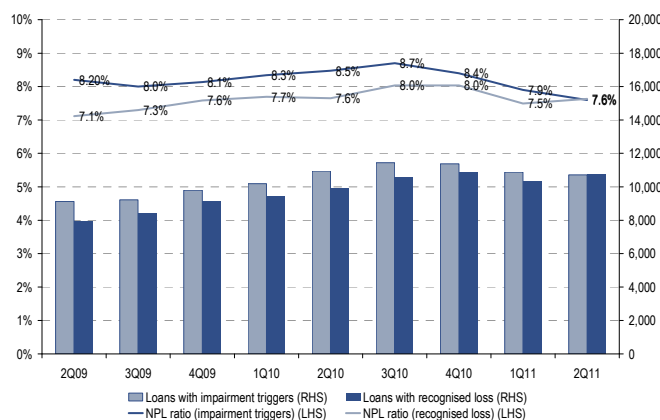
Source: Company reports, Citi Investment Research and Analysis

Figure 40. PKO BP – Net Fees by Divisions, 1Q07-2Q11 (Polish Zloty in million)



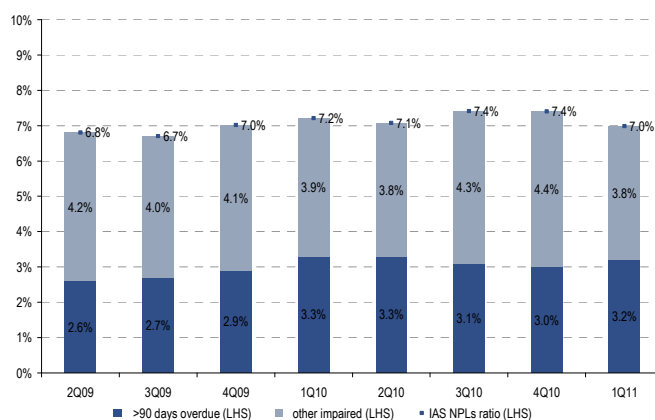
Source: Company reports, Citi Investment Research and Analysis

Figure 41. PKO BP – Consolidated Impaired Loans, 2Q09-2Q11



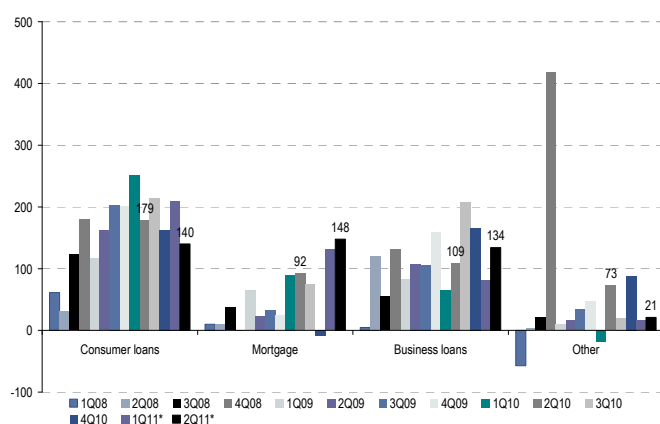
Source: Company reports, Citi Investment Research and Analysis

Figure 42. PKO BP – Unconsolidated Impaired Loans, 2Q09-1Q11



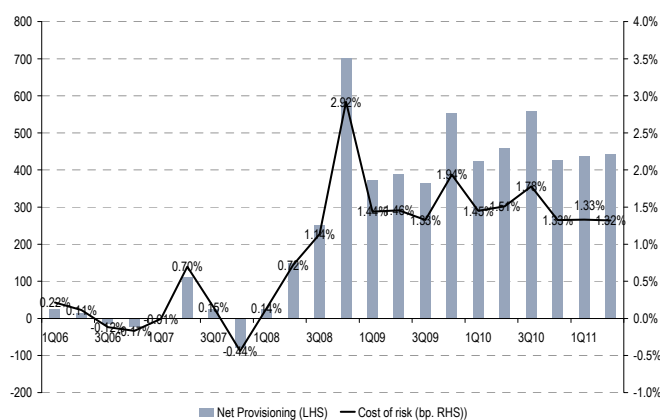
Source: Company reports, Citi Investment Research and Analysis

Figure 43. PKO BP – Provisioning Breakdown, 1Q08-2Q11 (Polish Zloty in million)



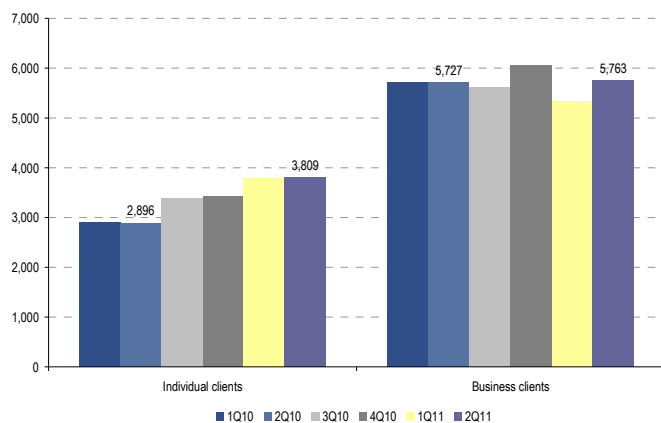
Source: Company reports, Citi Investment Research and Analysis

Figure 44. PKO BP – Cost of Risk, 1Q06-2Q11 (Polish Zloty in million/Percentage)



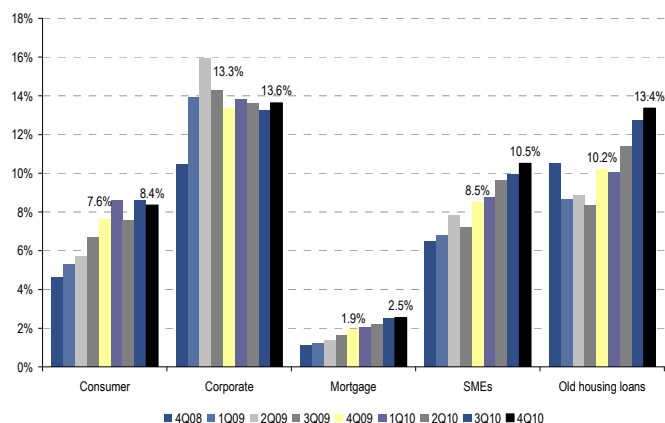
Source: Company reports, Citi Investment Research and Analysis

Figure 45. PKO BP --- NPL Volumes By Segment, 4Q08-2Q11



Source: Company reports, Citi Investment Research and Analysis

Figure 46. PKO BP --- NPL Ratios By Products, 4Q08-4Q10 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 47. PKO BP – Segment Breakdown*, 1Q07-2Q11 (Polish Zloty in million)

	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Nil	1,000	1,054	1,276	1,317	1,427	1,576	1,593	1,618	1,193	1,108	1,332	1,417	1,474	1,623	1,719	1,731	1,719	1,855
Retail	830	883	1,233	1,185	1,133	1,454	1,475	1,501	1,213	1,330	1,409	1,365	1,218	1,550	1,514	889	1,318	1,376
Corporate	55	59	78	66	64	159	60	136	129	118	188	206	165	225	194	53	152	146
Investment and Treasury	50	27	115	66	143	-37	58	-19	-238	-250	-264	-154	61	-153	11	789	66	50
Other	65	85	-150	0	87	0	0	0	89	-89	0	0	31	0	0	0	184	283
Fees	478	486	726	642	600	478	605	612	550	622	701	710	725	802	798	818	737	804
Retail	532	573	393	577	647	417	550	505	543	480	623	619	648	710	695	686	653	713
Corporate	40	40	18	41	44	40	32	82	54	50	57	61	56	60	75	96	64	63
Investment and Treasury	34	38	21	24	25	21	23	25	20	25	21	29	22	31	27	36	20	28
Other	-128	-165	293	0	-116	0	0	0	-67	67	0	0	0	0	0	0	0	0
Total Income	1,622	1,734	2,122	2,225	2,162	2,237	2,413	2,543	2,145	2,190	2,206	2,328	2,346	2,561	2,690	2,652	2,581	2,735
Retail	1,452	1,482	1,857	1,988	1,921	2,044	2,234	2,260	1,865	2,222	2,007	2,072	1,919	2,346	2,319	1,567	2,045	2,143
Corporate	108	97	137	127	129	255	136	270	220	258	227	316	237	308	300	156	240	231
Investment and Treasury	187	292	-134	111	235	-62	43	14	93	-323	-28	-60	139	-93	71	930	123	133
Other	-125	-136	261	0	-123	0	0	0	-33	33	0	0	52	0	0	0	172	228
Total costs	-824	-890	-1,085	-1,242	-948	-1,037	-1,047	-1,238	-1,082	-994	-1,029	-1,140	-1,014	-1,021	-1,057	-1,157	-1,054	-1,069
Retail	-795	-839	-1,011	-1,149	-888	-940	-957	-1,121	-992	-894	-975	-1,046	-916	-934	-958	-1,044	-950	-960
Corporate	-21	-41	-62	-62	-63	-69	-65	-86	-55	-82	-41	-72	-62	-70	-70	-84	-69	-75
Investment and Treasury	-8	-10	-12	-31	-22	-27	-25	-32	-24	-29	-13	-22	-36	-17	-30	-29	-35	-34
Other	0	0	0	0	25	0	0	0	-11	11	0	0	0	0	0	0	0	0
Cost/Income	51%	51%	51%	56%	44%	46%	43%	49%	50%	45%	47%	49%	43%	40%	39%	44%	41%	39%
Retail	55%	57%	54%	58%	46%	46%	43%	50%	53%	40%	49%	51%	48%	40%	41%	67%	46%	45%
Corporate	20%	42%	45%	49%	49%	27%	48%	32%	25%	32%	18%	23%	26%	23%	23%	54%	29%	32%
Investment and Treasury	4%	3%	-9%	28%	10%	-44%	58%	232%	25%	-9%	-46%	-36%	26%	-18%	42%	3%	28%	26%
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Operating income	798	844	1,037	983	1,213	1,200	1,366	1,305	1,063	1,196	1,177	1,189	1,332	1,540	1,633	1,496	1,527	1,666
Retail	657	643	846	838	1,033	1,104	1,277	1,139	873	1,329	1,032	1,025	1,002	1,413	1,361	523	1,096	1,183
Corporate	87	56	75	65	66	185	71	184	165	177	187	245	175	237	230	72	171	156
Investment and Treasury	179	282	-146	80	212	-89	18	-18	69	-353	-41	-82	103	-110	41	901	88	98
Other	-125	-136	261	0	-98	0	0	0	-43	43	0	0	52	0	0	0	172	228
Net provisioning	-9	-102	-26	81	-21	-149	-252	-583	-374	-390	-364	-553	-425	-458	-559	-426	-438	-443
Retail	-44	-47	-139	40	-80	-57	-226	-436	-270	-352	-268	-388	-386	-387	-406	-317	-399	-375
Corporate	53	-61	90	0	6	-106	-28	-71	-73	-58	-106	-157	-39	-64	-102	-123	-42	-64
Investment and Treasury	-10	11	8	-9	48	14	2	-79	2	-13	10	-8	0	-6	-51	14	3	-4
Other	-8	-6	14	50	6	0	0	3	-32	33	0	0	0	0	0	0	0	0
Pre-tax profit	873	742	929	1,067	1,196	1,064	1,116	718	695	801	813	636	907	1,082	1,074	1,069	1,088	1,223
Retail	675	634	607	879	952	1,047	1,050	703	603	977	763	638	616	1,025	956	206	696	808
Corporate	145	-2	158	64	72	79	44	113	92	119	81	88	136	173	129	-51	129	92
Investment and Treasury	236	335	-246	71	260	-76	20	-97	71	-366	-32	-90	103	-116	-10	914	91	94
Other	-183	-225	409	54	-88	13	2	-1	-70	71	0	0	52	0	0	0	172	228

* 1Q10 and 1Q11 according to the new methodology, not fully comparable with other periods.

Source: Company reports, Citi Investment Research and Analysis

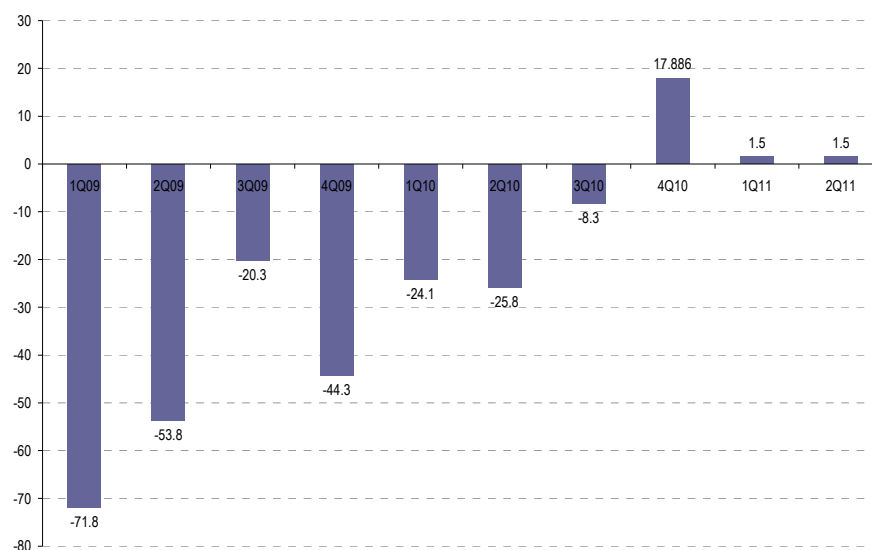
Figure 48. PKO BP – Ukrainian Business*, 1Q09-2Q11 (Polish Zloty in million)

	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
NII	42	45	20	48	19	22	18	11	15	8
F&C	11	14	15	2	8	11	11	10	9	9
Financial and other income	7	-2	-7	4	-4	-5	-1	9	1	3
Total income	60	57	28	54	24	28	28	29	25	20
Costs	-36	-33	-27	-32	-27	-30	-26	-32	-25	-23
Operating income	24	24	1	23	-3	-2	2	-2	0	-3
Provisions	-81	-98	-30	-68	-24	3	-1	12	8	4
Pre-tax profit	-57	-75	-28	-45	-27	1	1	10	8	1

* Includes Kredobank and Ukrpolinwestycje results.

Source: Company reports, Citi Investment Research and Analysis

Figure 49. PKO BP – Kredobank Net Profit/Loss, 1Q09-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Annual Financials

Figure 50. PKO BP – Profit and Loss, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg (%)	2007	chg (%)	2008	chg (%)	2009	chg (%)	2010	chg (%)	2011E	chg (%)	2012E	chg (%)
Net Interest Income	3,544	3,832	8.1%	4,644	21.2%	6,127	31.9%	5,051	-17.6%	6,516	29.0%	7,367	13.1%	7,784	5.7%
Net Fee & Commission Income	1,218	1,866	53.2%	2,335	25.1%	2,412	3.3%	2,583	7.1%	3,143	21.7%	3,199	1.8%	3,478	8.7%
Financial Income	309	-40	NA	-65	60.2%	-166	155.3%	58	NA	10	-82.0%	25	135.3%	88	256.8%
Other Income	1,395	860	-38.4%	830	-3.5%	1,015	22.3%	1,175	15.8%	528	-55.1%	448	-15.2%	486	8.5%
Total Revenue	6,466	6,518	0.8%	7,744	18.8%	9,388	21.2%	8,868	-5.5%	10,198	15.0%	11,039	8.2%	11,836	7.2%
Labour Costs	-2,053	-2,255	9.9%	-2,289	1.5%	-2,429	6.1%	-2,308	-5.0%	-2,375	2.9%	-2,376	0.1%	-2,491	4.8%
General Costs	-1,642	-1,239	-24.5%	-1,413	14.1%	-1,437	1.7%	-1,467	2.1%	-1,362	-7.2%	-1,510	10.9%	-1,627	7.7%
Depreciation	-467	-318	-31.9%	-381	19.7%	-430	13.0%	-469	9.1%	-512	9.2%	-514	0.3%	-557	8.4%
Operating Expenses	-4,161	-3,812	-8.4%	-4,083	7.1%	-4,296	5.2%	-4,244	-1.2%	-4,249	0.1%	-4,400	3.6%	-4,675	6.3%
Operating Profit	2,305	2,706	17.4%	3,662	35.3%	5,092	39.1%	4,624	-9.2%	5,948	28.6%	6,638	11.6%	7,161	7.9%
Provision Charge	-161	-1	-99.6%	-57	8601%	-1,130	1896%	-1,681	48.7%	-1,868	11.1%	-1,755	-6.1%	-2,365	34.8%
Associate Income	24	-4	NA	4	NA	16	256.7%	0	-97.8%	-1	NA	-2	120.5%	4	NA
Profit Before Tax	2,167	2,701	24.7%	3,609	33.6%	3,977	10.2%	2,943	-26.0%	4,079	38.6%	4,882	19.7%	4,800	-1.7%
Minorities	-21	-58	180.7%	-38	-35.3%	-19	-51.0%	-6	-66.3%	4	NA	3	-20.2%	4	19.5%
Tax	-411	-494	20.1%	-668	35.2%	-838	25.5%	-631	-24.7%	-866	37.2%	-959	10.7%	-912	-4.9%
Other	0	0	NA	0	NA	0	NA	0	NA	0	NA	0	NA	0	NA
Net Profit	1,735	2,149	23.9%	2,904	35.1%	3,121	7.5%	2,306	-26.1%	3,217	39.5%	3,926	22.0%	3,892	-0.9%
EPS (Zl)	1.60	1.98	23.9%	2.68	35.1%	2.88	7.5%	2.07	-28.0%	2.57	24.1%	3.14	22.0%	3.11	-0.9%
DPS (Zl)	0.74	0.90	22.5%	1.01	11.2%	0.92	-8.3%	1.90	105.9%	1.98	4.2%	0.63	-68.3%	0.62	-0.9%
Average Diluted Number of Shares (m)	1,084	1,084	0.0%	1,084	0.0%	1,084	0.0%	1,112	2.6%	1,250	12.4%	1,250	0.0%	1,250	0.0%

Source: Company reports, CIRA estimates

Figure 51. PKO BP – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg (%)	2007	chg (%)	2008	chg (%)	2009	chg (%)	2010	chg (%)	2011E	chg (%)	2012E	chg (%)
Cash and NBP Balances	3,895	4,628	18.8%	4,683	1.2%	5,837	24.6%	7,094	21.5%	6,182	-12.9%	6,275	1.5%	6,369	1.5%
Interbank placements	12,663	13,431	6.1%	5,261	-60.8%	3,364	-36.1%	2,023	-39.9%	2,307	14.0%	2,353	2.0%	2,400	2.0%
Financial Assets & Securities	23,929	20,480	-14.4%	16,790	-18.0%	18,264	8.8%	24,557	34.5%	24,200	-1.5%	28,220	16.6%	28,821	2.1%
Net client lending	46,875	58,907	25.7%	76,417	29.7%	101,108	32.3%	116,573	15.3%	130,668	12.1%	143,943	10.2%	155,809	8.2%
Fixed assets	3,332	3,599	8.0%	4,004	11.2%	4,317	7.8%	4,350	0.8%	4,378	0.6%	4,636	5.9%	4,914	6.0%
Other assets	918	982	6.9%	1,383	40.9%	1,746	26.3%	1,881	7.8%	1,924	2.3%	2,231	16.0%	2,432	9.0%
Total Assets	91,613	102,026	11.4%	108,538	6.4%	134,636	24.0%	156,479	16.2%	169,661	8.4%	187,658	10.6%	200,745	7.0%
Interbank borrowing	2,084	4,353	108.9%	4,704	8.1%	6,991	48.6%	5,153	-26.3%	5,237	1.6%	5,761	10.0%	6,049	5.0%
Client deposits	76,748	83,507	8.8%	86,580	3.7%	102,939	18.9%	125,073	21.5%	132,981	6.3%	145,422	9.4%	157,410	8.2%
Other liabilities	4,007	3,985	-0.5%	5,275	32.4%	10,707	103.0%	5,817	-45.7%	10,082	73.3%	13,748	36.4%	11,456	-16.7%
Minorities	44	102	133.6%	58	-43.2%	46	-20.4%	7	-84.1%	2	-72.8%	-1	NA	-4	543.6%
Equity (ex Minorities)	8,731	10,078	15.4%	11,921	18.3%	13,952	17.0%	20,429	46.4%	21,358	4.5%	22,728	6.4%	25,835	13.7%
Total liabilities & Equity	91,613	102,026	11.4%	108,538	6.4%	134,636	24.0%	156,479	16.2%	169,661	8.4%	187,658	10.6%	200,745	7.0%
Interest Earning Assets	87,363	97,445	11.5%	103,151	5.9%	128,662	24.7%	150,247	16.8%	163,358	8.7%	180,791	10.7%	193,399	7.0%
BVPS (Zl)	8.10	9.39	16.0%	11.05	17.7%	12.92	16.9%	16.35	26.6%	17.09	4.5%	18.18	6.4%	20.67	13.7%

Source: Company reports, CIRA estimates

Figure 52. PKO BP – Key Ratios, 2005-2012E (Percentage)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	4.16%	4.15%	4.63%	5.29%	3.62%	4.16%	4.28%	4.16%
NIM on Total Ave. Assets	3.93%	3.96%	4.41%	5.04%	3.47%	4.00%	4.12%	4.01%
Net Fee & Commission Income/Total Income	18.8%	28.6%	30.2%	25.7%	29.1%	30.8%	29.0%	29.4%
Net Fee & Commission Income/Deposits	1.6%	2.2%	2.7%	2.3%	2.1%	2.4%	2.2%	2.2%
Cost/Income	64.4%	58.5%	52.7%	45.8%	47.9%	41.7%	39.9%	39.5%
Cost/Avg. Assets	4.6%	3.9%	3.9%	3.5%	2.9%	2.6%	2.5%	2.4%
Effective tax rate	19.0%	18.3%	18.5%	21.1%	21.5%	21.2%	19.6%	19.0%
Dividend Payout Ratio	46.1%	45.6%	37.5%	32.0%	103.0%	76.9%	20.0%	20.0%
Provisions/Avg Net Loans	0.36%	0.00%	0.08%	1.27%	1.54%	1.51%	1.28%	1.58%
Equity/Assets	9.6%	10.0%	11.0%	10.4%	13.1%	12.6%	12.1%	12.9%
Loans/Deposits	61.1%	70.5%	88.3%	98.2%	93.2%	98.3%	99.0%	99.0%
Loans/Total Assets	51.2%	57.7%	70.4%	75.1%	74.5%	77.0%	76.7%	77.6%
ROE	20.7%	22.9%	26.4%	24.1%	13.4%	15.4%	17.8%	16.0%
ROA	1.92%	2.22%	2.76%	2.57%	1.58%	1.97%	2.20%	2.00%
NPLs/Total Loans	6.80%	4.31%	3.19%	3.67%	8.13%	8.40%	8.50%	7.80%
Provision Coverage of NPLs	NA	NA	96.2%	76.4%	40.2%	42.7%	44.7%	55.2%
RWA/Total Assets	50.8%	58.8%	76.5%	84.7%	77.1%	83.3%	82.0%	85.0%
Tier I Ratio (%)	13.9%	11.6%	10.2%	9.9%	13.5%	11.3%	11.3%	10.6%
CAR	13.9%	11.8%	12.0%	11.3%	14.8%	12.5%	12.3%	11.5%
Bank Employees	33,479	31,955	30,659	29,064	31,098	29,780	29,534	28,948

Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Buy/Low Risk	1L
Price (29 Sep 11)	ZL133.00
Target price	ZL171.00
from ZL190.00	
Expected share price return	28.6%
Expected dividend yield	6.8%
Expected total return	35.3%
Market Cap	ZL34,895M
	US\$10,632M

Price Performance (RIC: BAPE.WA, BB: PEO PW)



Bank Pekao SA (BAPE.WA)

Defensive: Maintaining Buy

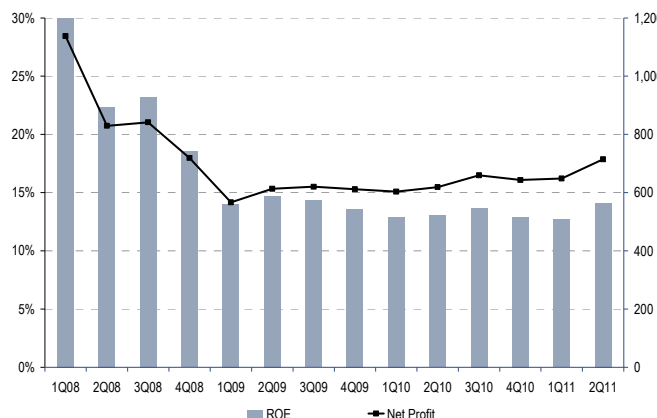
- **Strategy Starts to Work** — Since the beginning of 2010 Pekao promised to accelerate lending, especially in core areas (Zloty mortgages, consumer loans and lending to SMEs) but finally, starting from 2H10, it has started to deliver on its promise. Rising lending leads to improvement in NIM.
- **Rising Retail Provisioning** — In 2Q11, due to 18% yoy higher NII, the pre-tax profit of the retail banking division increased 38% yoy. We note, however, that in 1Q11 and 2Q11 retail provisioning rose qoq (reversing the trend seen in 2H10 and going against industry trends), signaling a risk that accelerated lending may lead to higher cost of risk in the future.
- **Pekao Interested in M&A...** — KBC officially announced it would like to sell Kredyt Bank, while BCP has confirmed it is looking for a buyer for Millennium and that it has received 3 written offers and a few additional verbal signs of interest. Luigi Lovaglio, Pekao's CEO, indicated at its post 2Q11 result analyst meeting that the bank is interested in M&A and is analysing which bank may be the best target. According to the *Gazeta Wyborcza* daily, Pekao placed an offer for Millennium while KBC is in bilateral negotiations with Santander regarding the sale of Kredyt Bank. None of the companies in question has commented on the reports.
- **UniCredit Ballast** — With c. ZL 8bn in surplus capital, Pekao has the firepower to make an acquisition. However, the capital position of UniCredit may be the largest obstacle to doing a deal. On the other hand, we note that a potential acquisition of 100% of Millennium at 1.8x book would decrease UniCredit's Tier 1 by just 35bp.
- **2012E EPS Cut by 25%** — We reduce our NIM estimate to 3.25% from 3.60% in 2012 and in 2013, lower our loan growth forecasts to 9% from 12% (in both years) and increase our cost of risk to 120bp from 70bp in both years. These changes lead us to cut our EPS estimates by 25% and 26%, respectively.
- **Maintaining Buy** — We maintain our assumption of sustainable ROE of 16% on reported equity and 21% on normalised capital. In setting our target price, we apply 50%/50% weights to both valuation approaches. Due to reduced 2012 and 2013 EPS estimates, we reduce our target price to ZL 171 from ZL 190 and maintain our Buy/Low Risk rating.

Bank Pekao SA (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	2,411.7	2,525.6	2,761.1	2,344.3	2,612.1
Diluted EPS (ZL)	9.20	9.63	10.52	8.94	9.96
Diluted EPS (Old) (ZL)	9.20	9.63	10.52	11.94	13.54
PE (x)	14.5	13.8	12.6	14.9	13.4
P/BV (x)	1.9	1.7	1.6	1.6	1.7
DPS (ZL)	2.90	6.80	9.00	11.00	12.00
Net Div Yield (%)	2.2	5.1	6.8	8.3	9.0
ROE (%)	14.1	13.1	13.3	11.1	12.4

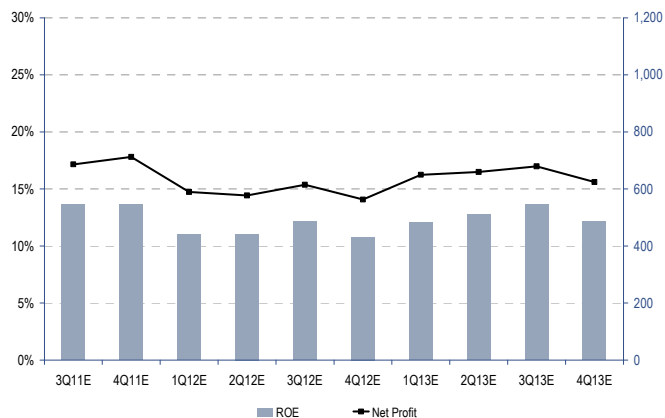
Bank Pekao in Snapshots

Figure 53. Bank Pekao – Reported Net Profit and ROE, 1Q08-2Q11
(Polish Zloty in million/Percentage)



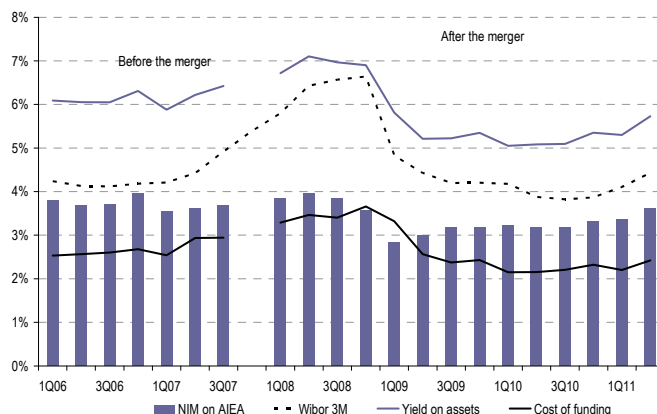
Source: Company reports, Citi Investment Research and Analysis

Figure 54. Bank Pekao – Forecast Net Profit and ROE, 3Q11-4Q13E
(Polish Zloty in million/Percentage)



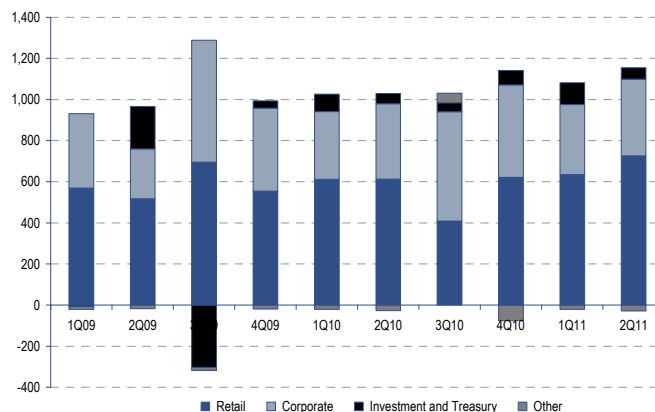
Source: Citi Investment Research and Analysis

Figure 55. Bank Pekao – Yield on Assets and Cost of Funding, 1Q06-2Q11 (Percentage)



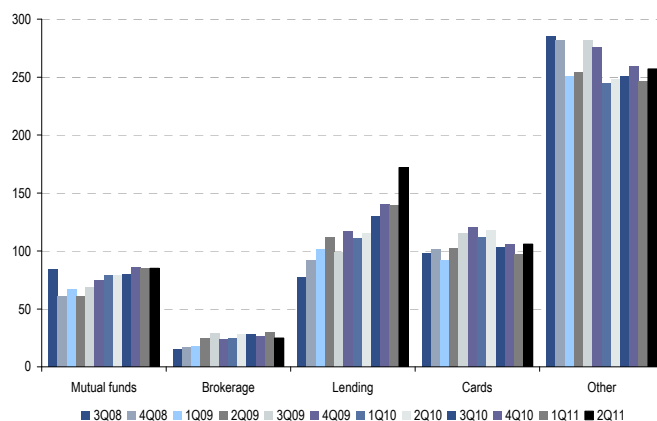
Source: Company reports, Citi Investment Research and Analysis

Figure 56. Bank Pekao – NII by Divisions, 1Q09-2Q11 (Polish Zloty in million)



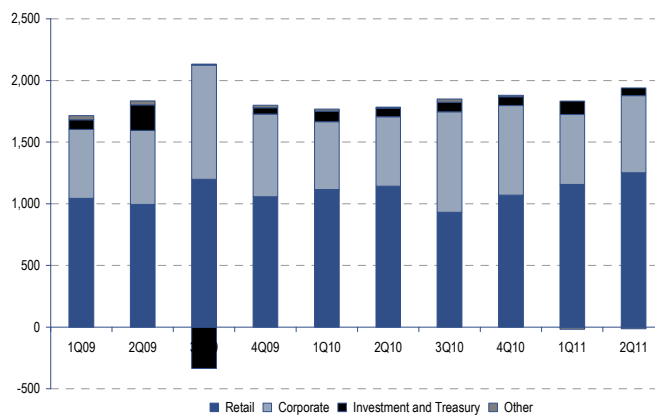
Source: Company reports, Citi Investment Research and Analysis

Figure 57. Bank Pekao – Breakdown of Net Fees, 3Q08-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Figure 58. Bank Pekao – Total Revenues by Divisions, 1Q09-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 59. Bank Pekao – Segment Breakdown, 1Q08 – 2Q11 (Polish Zloty in million)

	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
NII	1,160.2	1,178.4	1,159.4	1,121.6	922.7	966.3	985.2	993.3	1,026	1,029	984	1,141	1,082	1,154
Retail	763.7	665.5	719.8	693.9	569.1	516.5	695.4	554.8	611.8	612.8	408.5	621.8	635.0	725.2
Corporate	385.0	2.7	202.2	203.7	361.5	243.6	593.0	403.3	330.2	366.7	531.9	449.4	340.4	374.7
Investment and Treasury	11.5	510.2	237.4	224.0	-7.9	206.2	-303.2	35.2	83.9	49.4	43.4	70.0	106.5	54.3
Other	-37.5	-36.0	-24.5	-12.1	-13.1	-18.1	-15.0	-19.0	-20.8	-26.4	47.2	-76.2	-20.7	-28.7
Total Income	1,936.5	1,969.7	2,020.9	1,906.6	1,682.0	1,802.2	1,790.4	1,778.0	1,750.9	1,774.9	1,823.4	1,868.8	1,833.3	1,938.7
Retail	1,265.5	1,223.4	1,234.3	1,183.2	1,045.0	995.3	1,199.1	1,057.2	1,114.9	1,142.7	931.2	1,069.8	1,156.1	1,251.6
Corporate	639.8	141.6	417.5	359.0	558.7	600.1	925.6	671.2	550.0	563.8	814.3	726.0	567.0	624.5
Investment and Treasury	31.2	604.7	369.1	364.3	78.3	206.8	-334.3	49.6	86.0	68.5	77.9	73.0	110.2	62.6
Other	-31.3	56.2	-10.9	39.0	32.2	32.4	7.9	20.5	16.0	8.9	25.8	9.9	-16.6	-12.5

Source: Company Reports, Citi Investment Research and Analysis

Figure 60. Bank Pekao – OJSC UniCredit Bank in Ukraine, 3Q08-2Q11 (Polish Zloty in million)

	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Operating income	54	79	67	63	66	55	52	49	58	37	45	37
Net Profit	8	18	1	2	4	8	12	8	10	7	14	12
Gross loans	3011	3393	3572	3318	2922	2806	2723	2844	2440	2518	2261	2051
Gross deposits	621	585	670	551	509	543	555	897	814	763	795	781

Source: Company Reports, Citi Investment Research and Analysis

Annual Financials

Figure 61. Bank Pekao – Profit and Loss, 2005-2012E (Polish Zloty in million)

GROUP	2005	chg	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	2,350	4.0%	2,379	1.2%	2,718	14.2%	4,509	65.9%	3,802	-15.7%	4,104	7.9%	4,477	9.1%	4,407	-1.6%
Net Fee & Commission Income	1,587	2.9%	1,856	16.9%	2,161	16.5%	2,342	8.3%	2,289	-2.3%	2,368	3.5%	2,542	7.3%	2,747	8.1%
Financial Income	405	na	380	-6.2%	390	2.6%	649	66.5%	827	27.6%	740	-10.5%	580	-21.6%	668	15.1%
Other Income	71	na	43	-39.8%	89	107.5%	351	295.8%	242	-31.3%	66	-72.5%	73	10.5%	80	9.0%
Total Revenue	4,413	2.7%	4,658	5.5%	5,358	15.0%	7,851	46.5%	7,160	-8.8%	7,279	1.7%	7,672	5.4%	7,902	3.0%
Labour Costs	-1,212	6.6%	-1,209	-0.2%	-1,397	15.6%	-1,875	34.1%	-1,856	-1.0%	-1,950	5.1%	-2,039	4.5%	-2,086	2.3%
General Costs	-812	-17.6%	-820	1.0%	-1,000	22.0%	-1,513	51.3%	-1,388	-8.2%	-1,314	-5.3%	-1,349	2.6%	-1,512	12.1%
Depreciation	-323	3.2%	-318	-1.4%	-339	6.4%	-414	22.2%	-441	6.6%	-392	-11.3%	-379	-3.2%	-405	6.9%
Operating Expenses	-2,346	-3.6%	-2,347	0.0%	-2,737	16.6%	-3,802	38.9%	-3,686	-3.0%	-3,656	-0.8%	-3,767	3.0%	-4,003	6.3%
Operating Profit	2,067	10.9%	2,311	11.8%	2,621	13.4%	4,050	54.5%	3,474	-14.2%	3,622	4.3%	3,906	7.8%	3,899	-0.2%
Provision Charge	-237	-32.9%	-222	-6.4%	-192	-13.5%	-263	36.7%	-535	103.3%	-589	10.1%	-563	-4.4%	-1,073	90.7%
Associate Income	44	na	91	105.7%	153	68.3%	123	-19.5%	58	-52.8%	68	17.6%	74	8.6%	83	11.8%
Profit Before Tax	1,874	19.6%	2,179	16.3%	2,582	18.5%	3,910	51.4%	2,997	-23.3%	3,102	3.5%	3,417	10.2%	2,909	-14.9%
Tax	-339	48.9%	-409	20.7%	-438	7.0%	-722	64.9%	-576	-20.2%	-571	-0.9%	-645	12.9%	-553	-14.3%
Profit After Tax	1,535	14.6%	1,771	15.4%	2,144	21.1%	3,188	48.7%	2,421	-24.1%	2,531	4.5%	2,772	9.5%	2,356	-15.0%
Extraordinary Income	0	na	19	na	18	na	353	na	0	na	0	na	0	na	0	na
Minorities	3	na	-2	na	-7	219.4%	-13	85.3%	-10	-25.9%	-5	-46.9%	-11	115.9%	-12	8.9%
Net Profit	1,538	na	1,788	16.2%	2,155	20.6%	3,528	63.7%	2,412	-31.6%	2,525	4.7%	2,761	9.3%	2,344	-15.1%
Net Profit After Adjustments	1,538	na	1,768	15.0%	2,137	20.9%	3,175	48.6%	2,412	-24.0%	2,526	4.7%	2,761	9.3%	2,344	-15.1%
EPS (Zl)	9.2	14.4%	10.7	16.1%	12.3	15.0%	13.5	9.2%	9.2	-31.7%	9.6	4.7%	10.5	9.3%	8.9	-15.1%
DPS (Zl)	7.4	15.6%	9.0	21.6%	9.6	6.7%	0.0	na	2.9	na	6.8	134.5%	9.0	32.4%	11.0	22.2%
Average Diluted Number of Shares (m)	167	0.1%	167	0.1%	175	4.9%	262	49.9%	262	0.1%	262	0.0%	262	0.0%	262	0.0%

Source: Company reports, CIRA estimates

Figure 62. Bank Pekao – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	chg	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Cash and NBP Balances	3,581	39.3%	3,580	0.0%	5,122	43.1%	9,934	93.9%	9,620	-3.2%	5,969	-38.0%	6,268	5.0%	6,581	5.0%
Interbank placements	6,966	17.6%	10,513	50.9%	16,960	61.3%	7,909	-53.4%	7,203	-8.9%	6,259	-13.1%	6,572	5.0%	6,900	5.0%
Financial Assets & Securities	19,274	na	17,531	-9.0%	26,527	51.3%	27,185	2.5%	29,917	10.1%	33,197	11.0%	28,397	-14.5%	30,786	8.4%
Net client lending	28,224	2.3%	31,778	12.6%	66,658	109.8%	79,078	18.6%	76,380	-3.4%	77,804	1.9%	85,934	10.5%	93,018	8.2%
Fixed assets	1,441	na	1,445	0.3%	2,021	39.8%	1,906	-5.7%	1,822	-4.4%	1,822	0.0%	1,895	4.0%	1,970	4.0%
Other assets	2,486	na	2,856	14.8%	6,808	138.4%	5,929	-12.9%	5,673	-4.3%	9,040	59.3%	9,164	1.4%	9,868	7.7%
Total Assets	61,972	71.7%	67,704	9.2%	124,096	83.3%	131,941	6.3%	130,616	-1.0%	134,090	2.7%	138,229	3.1%	149,124	7.9%
Interbank borrowing	3,948	na	4,055	2.7%	9,942	145.2%	14,993	50.8%	8,479	-43.4%	7,641	-9.9%	8,405	10.0%	9,626	14.5%
Client deposits	46,848	10.7%	51,794	10.6%	89,944	73.7%	90,889	1.1%	97,250	7.0%	99,807	2.6%	101,235	1.4%	109,580	8.2%
Other liabilities	2,754	na	2,962	7.6%	9,463	219.4%	10,022	5.9%	6,516	-35.0%	6,385	-2.0%	7,308	14.5%	8,641	18.3%
Minorities	15	-10.9%	17	8.5%	81	380.8%	89	10.7%	83	-6.8%	83	-0.2%	87	4.8%	99	13.8%
Equity (ex Minorities)	8,407	6.6%	8,876	5.6%	14,667	65.2%	15,947	8.7%	18,288	14.7%	20,174	10.3%	21,195	5.1%	21,178	-0.1%
Total liabilities & Equity	61,972	23.4%	67,704	9.2%	124,096	83.3%	131,941	6.3%	130,616	-1.0%	134,090	2.7%	138,229	3.1%	149,124	7.9%
Interest Earning Assets	58,790	na	64,369	9.5%	72,737	13.0%	127,613	75.4%	126,224	-1.1%	126,267	0.0%	130,362	3.2%	140,636	7.9%
BVPS (Zl)	50	na	53	5.4%	56	5.3%	61	8.6%	70	14.7%	77	10.2%	81	5.1%	81	-0.1%

Source: Company reports, CIRA estimates

Figure 63. Bank Pekao – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	4.11%	3.86%	3.96%	3.67%	3.00%	3.25%	3.49%	3.25%
NIM on Total Ave. Assets	3.88%	3.67%	3.66%	3.52%	2.90%	3.10%	3.29%	3.07%
Net Fee & Commission Income/Total Income	36.0%	39.8%	40.3%	29.8%	32.0%	32.5%	33.1%	34.8%
Net Fee & Commission Income/Deposits	3.4%	3.6%	2.4%	2.6%	2.4%	2.4%	2.5%	2.5%
Cost/Income	53.2%	50.4%	51.1%	48.4%	51.5%	50.2%	49.1%	50.7%
Cost/Avg. Assets	3.87%	3.62%	3.69%	2.97%	2.81%	2.76%	2.77%	2.79%
Effective tax rate	18.1%	18.8%	16.9%	18.5%	19.2%	18.4%	18.9%	19.0%
Dividend Payout Ratio	80.1%	84.0%	116.8%	0.0%	31.5%	70.6%	85.5%	123.1%
Provisions/Avg Net Loans	0.85%	0.74%	0.52%	0.36%	0.69%	0.76%	0.69%	1.20%
Equity/Assets	13.6%	13.1%	11.9%	12.2%	14.1%	15.1%	15.4%	14.3%
Loans/Deposits	60.2%	61.4%	74.1%	87.0%	78.5%	78.0%	84.9%	84.9%
Loans/Total Assets	45.5%	46.9%	53.7%	59.9%	58.5%	58.0%	62.2%	62.4%
ROE	18.9%	20.7%	22.9%	23.0%	14.1%	13.1%	13.3%	11.1%
ROA	2.54%	2.76%	2.91%	2.76%	1.84%	1.91%	2.03%	1.63%
NPLs/Total Loans	15.6%	11.8%	7.8%	5.5%	6.8%	7.0%	7.0%	6.8%
Provision Coverage of NPLs	83.9%	87.3%	84.1%	87.2%	76.8%	72.7%	67.1%	74.7%
Tier 1 Ratio (%)	19.6%	16.5%	12.1%	12.2%	16.2%	17.6%	19.1%	17.2%
Group Employees	15,937	15,647	22,926	21,992	20,874	20,783	20,668	20,668

Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Rating Change
- Target Price Change
- Estimate Change

Buy/Medium Risk	1M
<i>from Hold/Medium Risk</i>	
Price (29 Sep 11)	ZL236.00
Target price	ZL298.00
<i>from ZL318.00</i>	
Expected share price return	26.3%
Expected dividend yield	5.6%
Expected total return	31.9%
Market Cap	ZL9,936M
	US\$3,027M

Price Performance (RIC: BREP.WA, BB: BRE PW)



BRE Bank SA (BREP.WA)

Time to Come Back to Corporate Roots: Upgrading to Buy

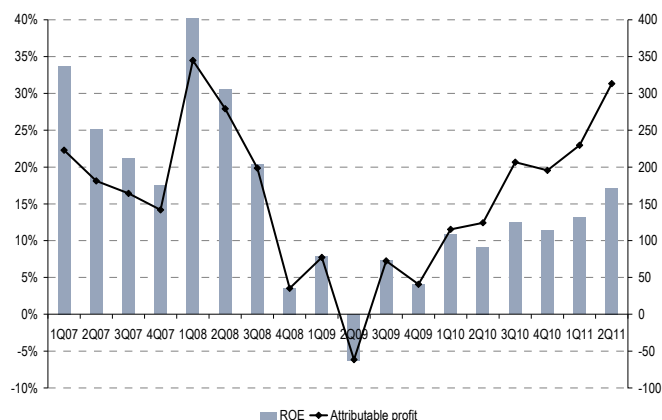
- **Bank's CHF Exposure Hedged, Clients' Not** — BRE's FX mortgage lending is well-managed in terms of the bank's risk as it is funded by CHF funding from Commerzbank and capitalised with CHF-denominated sub-debt but still the bank is exposed to rising credit risk as clients' liabilities (and thus also loan-to-value, LtV) and monthly installments rise. In our opinion, monthly installments matter much more than LtV and we expect that the material increase in the installments on FX mortgages that clients are seeing for the first time will lead to an acceleration of the current increase in mortgage NPLs (the NPL ratio grew to 1.1% in 2Q11 from 0.7% in 2Q10 and 0.4% in 2Q09).
- **Strong Retail Profits** — Even excluding the impact of the sales of NPLs, retail banking, due to rising NII and net fees (+34% yoy and +70% yoy), managed to become the main contributor to the bank's results and delivered 55% of revenues, 45% of administrative costs, 44% of provisioning and 72% of pre-tax profit in 2Q11.
- **Weak Corporate Banking** — On the other hand, corporate profits disappointed in 2Q11, with pre-provision profit rising just 6% yoy, negatively affected by a 2% decline in net fees and a large increase in administrative costs (+8% yoy vs. +7% growth in total revenues). Pre-tax earnings of the investment banking division declined 11% yoy due to the high base (ZI 17m gain on PZU shares in 2Q10).
- **2012E EPS Cut by 41%** — We reduce our NIM estimate to 2.18% from 2.39% in 2012 and to 2.17% from 2.38% in 2013, lower our loan growth forecasts to 4% from 16% in 2012 and 8% from 14% in 2013 and increase our cost of risk to 130bp from 80bp in 2012 and to 130bp from 75bp in 2013. These changes lead us to cut our EPS estimates by 41% and 47%, respectively.
- **Upgrading to Buy** — We maintain our assumption of sustainable ROE at 15.0% but due to reduced 2012 and 2013 EPS estimates we reduce our target price to ZI 298 from ZI 318 previously. Due to the recent correction in the share price, we upgrade the stock to Buy/Medium Risk (1M) from Hold/Medium Risk (2M).

BRE Bank SA (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	128.9	641.6	1,117.0	623.7	666.9
Diluted EPS (ZL)	3.83	16.95	26.55	14.82	15.85
Diluted EPS (Old) (ZL)	3.83	16.95	26.55	25.19	30.10
PE (x)	61.6	13.9	8.9	15.9	14.9
P/BV (x)	1.9	1.4	1.2	1.2	1.2
DPS (ZL)	0.00	0.00	13.27	13.34	14.27
Net Div Yield (%)	0.0	0.0	5.6	5.7	6.0
ROE (%)	3.2	11.6	14.9	7.7	8.1

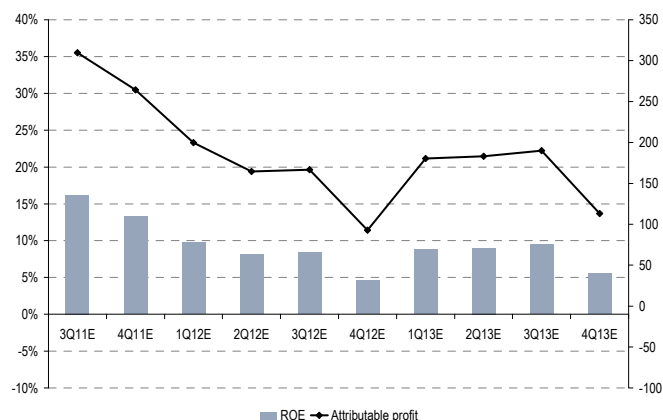
BRE Bank in Snapshots

Figure 64. BRE Bank – Reported Net Profit and ROE, 1Q07-2Q11
(Polish Zloty in million/Percentage)



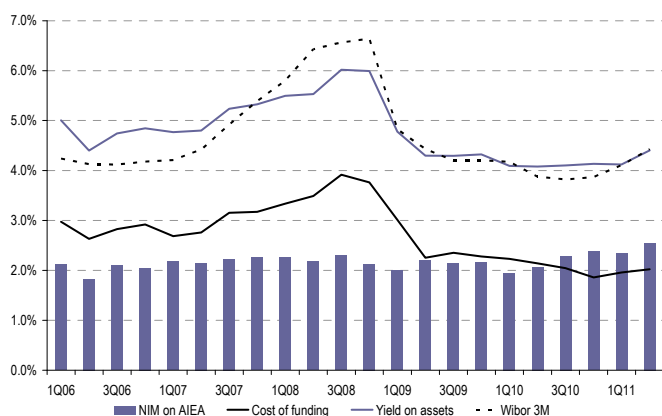
Source: Company reports, Citi Investment Research and Analysis

Figure 65. BRE Bank – Forecast Net Profit and ROE, 3Q11E-4Q13E
(Polish Zloty in million/Percentage)



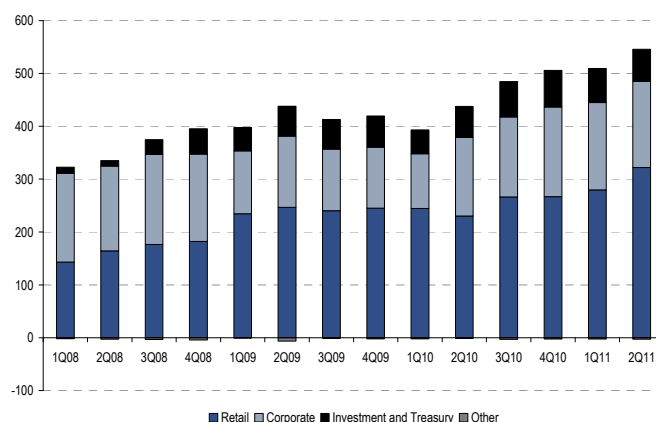
Source: Citi Investment Research and Analysis

Figure 66. BRE Bank – Yield on Assets and Cost of Funding, 1Q06-2Q11
(Percentage)



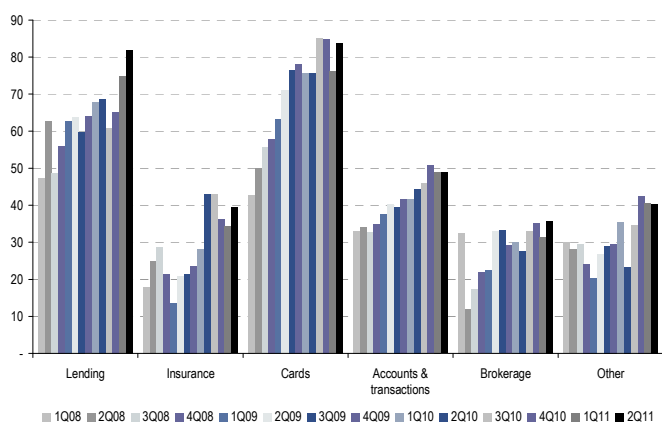
Source: Company reports, Citi Investment Research and Analysis

Figure 67. BRE Bank – NII by Divisions, 1Q08-2Q11 (Polish Zloty in million)



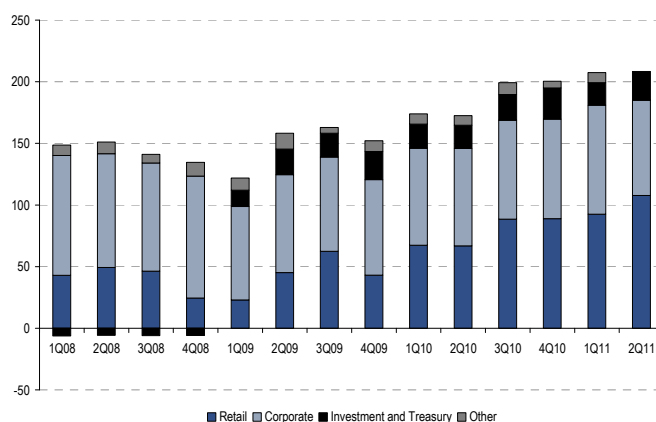
Source: Company reports, Citi Investment Research and Analysis

Figure 68. BRE Bank – Breakdown of Net Fees, 1Q08-2Q11 (Polish Zloty in million)



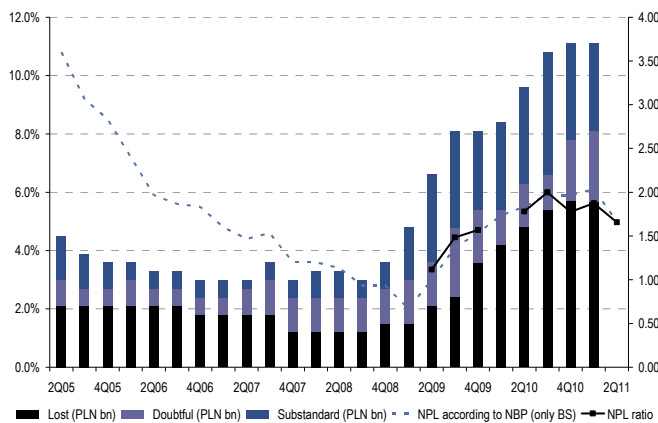
Source: Company reports, Citi Investment Research and Analysis

Figure 69. BRE Bank – Net Fees by Divisions, 1Q08-1Q11 (Polish Zloty in million)



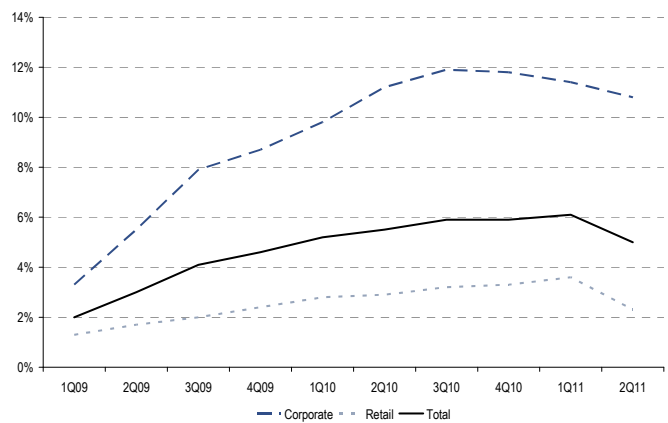
Source: Company reports, Citi Investment Research and Analysis

Figure 70. BRE Bank – NPL Ratios, 2Q05-2Q11



Source: Company reports, Citi Investment Research and Analysis

Figure 71. BRE Bank – Retail and Corporate NPL Ratios, 1Q09-2Q11



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 72. BRE Bank – Segment Breakdown, 1Q06 – 2Q11 (Polish Zloty in million)

	1Q06	2Q06	3Q06	4Q06	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Nil	177	165	200	205	231	246	272	295	321	332	371	391	397	431	412	418	391	436	481	503	507	542
Retail	61	69	80	85	96	106	116	125	143	164	176	182	235	247	240	245	244	230	267	267	280	322
Corporate	102	113	119	118	125	140	154	160	168	160	171	165	119	135	116	115	104	148	151	169	165	163
Investment and Treasury	13	-14	2	3	11	0	3	17	12	10	28	48	44	57	56	60	45	59	67	69	64	61
Other	1	-3	0	-1	0	0	0	-8	-2	-3	-3	-4	0	-6	-1	-2	-2	-1	-3	-3	-3	-3
Fees	90	94	104	124	143	147	139	136	142	145	135	129	122	158	163	152	174	172	199	200	207	208
Retail	15	16	28	43	49	49	47	45	43	49	46	24	23	45	62	43	67	67	88	89	93	108
Corporate	81	82	82	91	99	100	96	97	97	92	88	99	76	80	76	77	79	79	80	81	88	77
Investment and Treasury	-5	-4	-6	-6	-5	-3	-4	-6	-6	-6	-6	-6	13	21	19	23	20	19	21	25	18	23
Other	-1	-1	0	-4	0	0	0	0	8	9	7	11	10	13	5	9	8	8	10	5	8	0
Total Income	374	390	412	452	505	556	548	610	788	625	695	600	672	715	724	740	689	749	795	846	831	894
Retail	89	100	128	155	165	182	193	196	225	263	288	265	307	354	361	322	367	359	413	410	426	491
Corporate	224	244	234	259	271	310	309	307	328	316	334	262	229	218	233	325	217	261	273	305	289	281
Investment and Treasury	59	35	56	44	62	57	35	56	193	28	65	68	109	130	106	99	98	112	107	115	112	108
Other	3	11	-7	-6	7	7	10	52	41	17	9	5	27	13	25	-5	7	17	3	16	4	14
Total costs	-244	-249	-256	-281	-288	-322	-299	-370	-347	-367	-364	-472	-359	-363	-364	-458	-354	-392	-417	-455	-408	-429
Retail	-72	-79	-81	-95	-91	-115	-111	-150	-141	-153	-156	-216	-151	-162	-162	-212	-155	-181	-194	-224	-183	-194
Corporate	-152	-150	-155	-163	-173	-183	-167	-193	-179	-189	-183	-226	-156	-150	-149	-188	-148	-155	-168	-174	-170	-168
Investment and Treasury	-18	-17	-17	-20	-19	-19	-18	-22	-15	-16	-15	-20	-40	-43	-43	-52	-44	-47	-46	-48	-46	-50
Other	-3	-3	-3	-3	-5	-5	-2	-6	-11	-9	-11	-10	-11	-8	-10	-7	-7	-9	-9	-9	-9	-17
Cost/Income	65%	64%	62%	62%	57%	58%	54%	61%	44%	59%	52%	79%	53%	51%	50%	62%	51%	52%	52%	54%	49%	48%
Retail	81%	79%	63%	61%	55%	63%	58%	76%	62%	58%	54%	81%	49%	46%	45%	66%	42%	51%	47%	55%	43%	40%
Corporate	68%	61%	66%	63%	64%	59%	54%	63%	55%	60%	55%	86%	68%	69%	64%	58%	68%	59%	61%	57%	59%	60%
Investment and Treasury	30%	50%	31%	45%	31%	34%	51%	39%	8%	55%	23%	30%	37%	33%	41%	52%	45%	41%	44%	42%	41%	46%
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Operating income	130	142	155	171	216	234	250	240	441	258	331	128	313	352	360	281	335	358	379	391	423	466
Retail	17	21	47	60	74	68	82	46	84	110	132	49	156	192	199	110	212	177	220	186	243	297
Corporate	72	94	79	96	98	127	142	113	149	126	151	36	73	68	84	137	69	106	105	131	120	113
Investment and Treasury	41	17	39	24	43	38	17	34	178	13	50	48	69	87	63	47	53	66	60	67	66	58
Other	0	9	-10	-9	2	2	8	46	30	9	-2	-5	15	5	15	-13	0	8	-7	7	-5	-2
Pre-tax profit	108	131	148	165	210	235	215	203	419	213	261	-2	103	-87	111	82	158	154	250	265	309	407
Retail	11	11	43	49	69	57	71	30	68	87	95	-9	74	62	73	8	109	81	151	114	186	317
Corporate	55	93	77	102	95	135	119	95	144	103	132	-36	-48	-234	-32	46	2	4	45	82	56	39
Investment and Treasury	42	18	38	24	42	41	16	33	177	14	36	48	62	80	56	40	48	60	61	62	72	53
Other	-1	9	-10	-10	3	2	8	46	30	9	-2	-5	15	5	15	-13	0	8	-7	7	-5	-2

Source: Company Reports, Citi Investment Research and Analysis

Figure 73. BRE Bank – Foreign Operations of mBank, 4Q07-2Q11 (Polish Zloty in million)

	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Net Profit	-27.1	-16	-21.5	-19.3	-23.7	-24.5	-28.4	-21.7	-37.6	-15.5	-14.5	-12.2	-10.8	-6.7	-7.5
Loans	4	19	123	354	755	1,014	1,059	1,064	1,063	1,085	1,289	1,396	1,412	1,479	1,519
Deposits	30	833	1,758	2,291	3,321	3,835	4,373	4,548	4,680	4,438	4,245	3,950	3,672	3,656	3,653
Accounts	36	128	211	301	389	527	624	694	775	846	879	902	924	947	966
Clients	26	85	135	191	244	294	323	354	390	424	447	464	478	492	504

Source: Company Reports, Citi Investment Research and Analysis

Annual Financials

Figure 74. BRE Bank – Profit and Loss, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	651	724	11.3%	1,028	41.9%	1,392	35.5%	1,658	19.1%	1,811	9.2%	2,125	17.3%	2,019	-5.0%
Net Fee & Commission Income	338	416	23.1%	564	35.5%	552	-2.3%	595	7.8%	746	25.4%	861	15.4%	968	12.5%
Financial Income	17	68	294.8%	55	-18.6%	-35	na	-9	-73.3%	86	na	21	-75.7%	13	-37.7%
Other Income	327	416	27.4%	555	33.2%	640	15.4%	608	-5.0%	482	-20.7%	511	6.1%	531	3.8%
Total Revenue	1,333	1,625	21.9%	2,202	35.5%	2,549	15.7%	2,851	11.9%	3,125	9.6%	3,518	12.6%	3,530	0.4%
Labour Costs	-403	-476	18.0%	-629	32.1%	-739	17.6%	-645	-12.8%	-744	15.5%	-816	9.6%	-860	5.4%
General Costs	-365	-404	10.5%	-475	17.6%	-607	27.9%	-641	5.5%	-636	-0.7%	-674	6.0%	-786	16.6%
Depreciation	-138	-165	19.7%	-176	6.9%	-203	15.4%	-259	27.5%	-237	-8.7%	-244	3.0%	-260	6.7%
Operating Expenses	-906	-1,044	15.3%	-1,280	22.5%	-1,550	21.1%	-1,545	-0.3%	-1,617	4.7%	-1,734	7.2%	-1,907	9.9%
Operating Profit	427	581	36.0%	922	58.9%	999	8.3%	1,307	30.8%	1,507	15.4%	1,783	18.3%	1,623	-9.0%
Provision Charge	-79	-46	-41.7%	-77	67.1%	-269	250.4%	-1,097	307.6%	-635	-42.1%	-423	-33.4%	-862	103.9%
Associate Income	0	0	-76.1%	0	na	0	na	0	na	0	na	0	na	0	na
Profit Before Tax	348	534	53.8%	846	58.2%	730	-13.7%	209	-71.3%	873	316.7%	1,361	55.9%	761	-44.1%
Minorities	-20	-25	23.4%	-38	49.3%	-32	-15.0%	-2	-95.0%	-19	1,108%	-19	-3.6%	-20	7.7%
Tax	-65	-124	90.6%	-185	48.6%	-108	-41.3%	-79	-27.3%	-212	168.4%	-294	39.1%	-152	-48.3%
Discontinued operations (after tax)	-14	36	na	87	139.7%	268	209.7%	0	na	0	na	70	na	35	-50.0%
Net Profit	248	421	70.2%	710	68.6%	858	20.8%	129	-85.0%	642	397.6%	1,117	74.1%	624	-44.2%
EPS (Zl)	7.6	12.8	67.8%	21.2	66.1%	25.5	20.4%	3.8	-85.0%	16.9	342.1%	26.5	56.6%	14.8	-44.2%
DPS (Zl)	0.0	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	13.3	na	13.3	0.5%
Average Diluted Number of Shares (m)	32.6	33.0	1.4%	33.5	1.5%	33.6	0.3%	33.6	0.1%	37.9	12.6%	42.1	11.2%	42.1	0.0%

Source: Company reports, CIRA estimates

Figure 75. BRE Bank – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Cash and NBP Balances	1,816	3,743	106.1%	2,027	-45.9%	2,522	24.4%	3,796	50.5%	2,364	-37.7%	2,529	7.0%	2,706	7.0%
Interbank placements	4,668	2,844	-39.1%	2,090	-26.5%	6,104	192.1%	2,531	-58.5%	2,511	-0.8%	2,260	-10.0%	2,034	-10.0%
Financial Assets & Securities	7,401	7,985	7.9%	12,062	51.1%	15,760	30.7%	16,120	2.3%	21,555	33.7%	19,154	-11.1%	19,772	3.2%
Net client lending	15,376	23,045	49.9%	33,683	46.2%	52,142	54.8%	52,469	0.6%	59,370	13.2%	65,015	9.5%	67,655	4.1%
Fixed assets	559	580	3.9%	670	15.5%	814	21.5%	786	-3.4%	778	-1.1%	855	10.0%	941	10.0%
Other assets	2,919	4,134	41.6%	5,451	31.9%	5,262	-3.5%	5,323	1.1%	3,474	-34.7%	3,972	14.3%	4,193	5.6%
Total Assets	32,739	42,331	29.3%	55,983	32.3%	82,605	47.6%	81,024	-1.9%	90,051	11.1%	93,785	4.1%	97,301	3.7%
Interbank borrowing	4,257	7,972	87.3%	12,287	54.1%	28,791	134.3%	27,024	-6.1%	28,727	6.3%	31,169	8.5%	31,636	1.5%
Client deposits	20,349	24,670	21.2%	32,402	31.3%	37,750	16.5%	42,791	13.4%	47,420	10.8%	47,381	-0.1%	49,305	4.1%
Other liabilities	6,024	7,066	17.3%	7,853	11.1%	12,016	53.0%	6,938	-42.3%	6,827	-1.6%	7,051	3.3%	8,090	14.7%
Minorities	73	91	24.9%	117	27.8%	154	31.5%	151	-1.7%	168	11.3%	114	-32.0%	134	17.5%
Equity (ex Minorities)	2,035	2,531	24.3%	3,325	31.4%	3,894	17.1%	4,120	5.8%	6,909	67.7%	8,070	16.8%	8,135	0.8%
Total liabilities & Equity	32,739	42,331	29.3%	55,983	32.3%	82,606	47.6%	81,024	-1.9%	90,051	11.1%	93,785	4.1%	97,301	3.7%
Interest Earning Assets	30,778	40,319	31.0%	53,570	32.9%	79,973	49.3%	78,431	-1.9%	87,631	11.7%	90,972	3.8%	94,382	3.7%
BVPS (Zl)	62	76	21.2%	99	30.7%	116	17.0%	123	5.8%	164	34.0%	192	16.8%	193	0.8%

Source: Company reports, CIRA estimates

Figure 76. BRE Bank – Key Ratios, 2005-2012E (Percentage)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	2.19%	2.04%	2.19%	2.09%	2.09%	2.18%	2.38%	2.18%
NIM on Total Ave. Assets	2.06%	1.93%	2.09%	2.01%	2.03%	2.12%	2.31%	2.11%
Net Fee & Commission Income/Total Income	25.4%	25.6%	25.6%	21.6%	20.9%	23.9%	24.5%	27.4%
Net Fee & Commission Income/Deposits	1.7%	1.7%	1.7%	1.5%	1.4%	1.6%	1.8%	2.0%
Cost/Income	68.0%	64.3%	58.1%	60.8%	54.2%	51.8%	49.3%	54.0%
Cost/Avg. Assets	2.9%	2.8%	2.6%	2.2%	1.9%	1.9%	1.9%	2.0%
Effective tax rate	18.8%	23.2%	21.8%	14.9%	37.7%	24.3%	21.6%	20.0%
Dividend Payout Ratio	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	50.0%	90.0%
Provisions/Avg Net Loans	0.53%	0.24%	0.27%	0.63%	2.10%	1.14%	0.68%	1.30%
Equity/Assets	6.4%	6.2%	6.1%	4.9%	5.3%	7.9%	8.7%	8.5%
Loans/Deposits	75.6%	93.4%	104.0%	138.1%	122.6%	125.2%	137.2%	137.2%
Loans/Total Assets	47.0%	54.4%	60.2%	63.1%	64.8%	65.9%	69.3%	69.5%
ROE	12.8%	18.5%	24.3%	23.8%	3.2%	11.6%	14.9%	7.7%
ROA	0.78%	1.12%	1.44%	1.24%	0.16%	0.75%	1.22%	0.65%
NPLs/Total Loans	7.4%	4.2%	2.3%	2.2%	4.7%	5.3%	5.3%	5.0%
Provision Coverage of NPLs	72.0%	82.9%	85.3%	73.5%	76.7%	74.6%	73.5%	88.7%
RWA/Total Assets	62.8%	67.7%	69.8%	71.3%	67.2%	62.6%	62.6%	62.6%
Tier I Ratio (%)	6.7%	5.9%	5.7%	5.6%	6.6%	10.4%	12.0%	11.6%
CAR	11.1%	10.4%	10.2%	10.0%	11.5%	15.9%	17.2%	16.7%
Group Employees	4,297	5,159	5,785	6,133	5,566	6,018	6,315	6,441

Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Buy/Medium Risk	1M
Price (29 Sep 11)	ZL740.00
Target price	ZL886.00
from ZL930.00	
Expected share price return	19.7%
Expected dividend yield	1.8%
Expected total return	21.6%
Market Cap	ZL9,627M
	US\$2,933M

Price Performance (RIC: SLAS.WA, BB: BSK PW)



ING Bank Slaski SA (SLAS.WA) No More Rate Hikes: Maintaining Buy

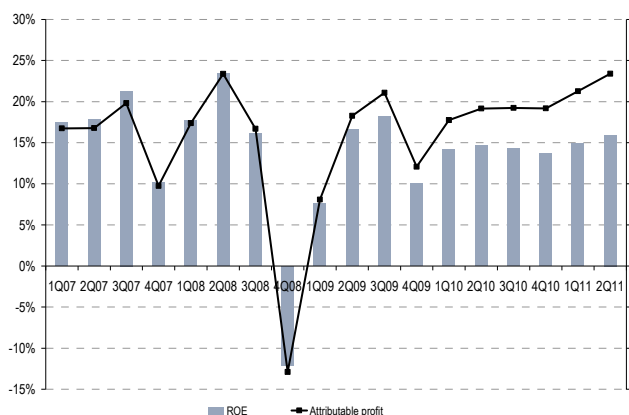
- **Improving Profitability in Retail Banking** — We appreciate ING BSK's continued growth in retail banking profits (pre-tax rising 25% yoy to ZL 112m in 2Q11), driven by rising NII (+18% yoy), more than offsetting a 18% decline in net fees. Improved profitability demonstrates that the bank's low-risk business model (local currency mortgages funded by retail deposits plus modern, low-cost transactional services) works.
- **Solid Corporate Banking** — Corporate banking also delivered solid 22% yoy growth in pre-tax profit, driven by increases of 9% yoy in NII and 46% yoy in net fees (due partly to low base).
- **Positive Evolution of Interest Rate Expectations** — Citi economists expect no more rate hikes this year and see a chance for rate cuts next year. Due to ING BSK's high exposure to fixed-income instruments and dependence on funding through saving accounts, leading to a relatively fixed yield on assets and a variable cost of funding, the bank is negatively exposed to rising interest rates, so the change in interest rate expectations is positive for the NIM outlook.
- **Limited CHF Exposure But High Operational Leverage** — Despite the very low share of CHF lending, the bank is indirectly exposed to CHF appreciation as, due to its high cost-to-risk ratio and high share of NII in total revenues, the bank's profitability depends to a high degree on the bank's NIM, which is impacted by the level of competition for deposits in the sector.
- **2012E EPS Estimates Cut by 22%** — We reduce our NIM estimate to 2.68% from 2.75% in 2012 and in 2013, lower our lending growth forecast to 10% from 13% in 2012 and maintain our 10% loan growth forecast in 2013. We increase our cost of risk to 120bp from 70bp (in both years). These changes lead us to cut our EPS estimates by 22% in each year.
- **Upgrading To Buy** — We maintain our assumption of sustainable ROE at 14.5% but due to lowered 2012 and 2013 EPS estimates we reduce our target price to ZL 886 from ZL 930 previously. Due to the bank's low exposure to CHF loans, its conservative business model and the lower probability of further rate hikes, we view the current price as attractive and maintain a Buy/Medium Risk (1M) rating.

ING Bank Slaski SA (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	595.1	753.1	886.3	740.0	832.0
Diluted EPS (ZL)	45.74	57.89	68.12	56.88	63.95
Diluted EPS (Old) (ZL)	45.74	57.89	70.24	73.16	82.21
PE (x)	16.2	12.8	10.9	13.0	11.6
P/BV (x)	2.0	1.7	1.5	1.4	1.3
DPS (ZL)	0.00	15.00	13.62	34.13	38.37
Net Div Yield (%)	0.0	2.0	1.8	4.6	5.2
ROE (%)	13.1	14.3	14.7	11.1	11.6

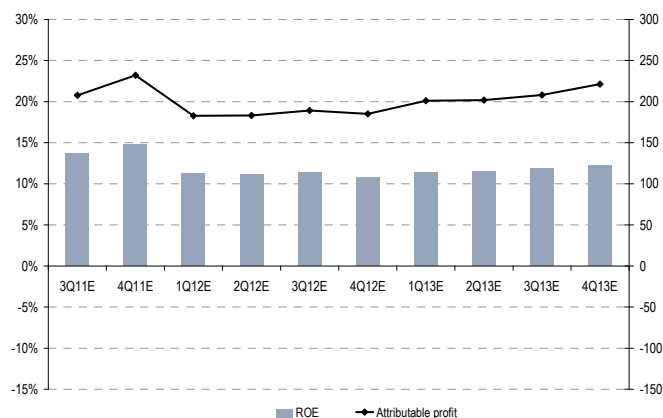
ING BSK in Snapshots

Figure 77. ING BSK – Reported Net Profit and ROE, 1Q07-2Q11 (Polish Zloty in million/Percentage)



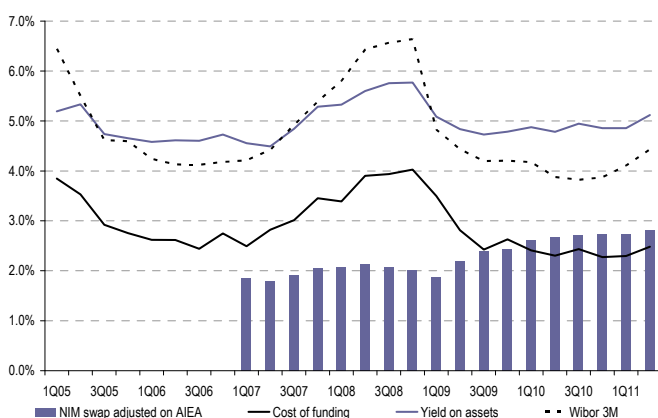
Source: Company reports, Citi Investment Research and Analysis

Figure 78. ING BSK – Forecast Net Profit and ROE, 3Q11-4Q13E (Polish Zloty in million/Percentage)



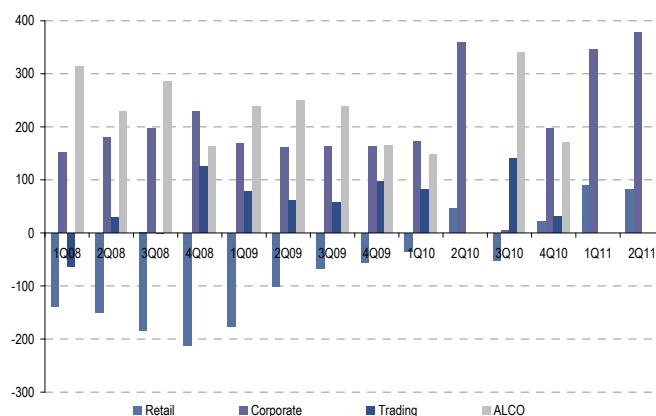
Source: Citi Investment Research and Analysis

Figure 79. ING BSK – Yield on Assets and Cost of Funding, 1Q05-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

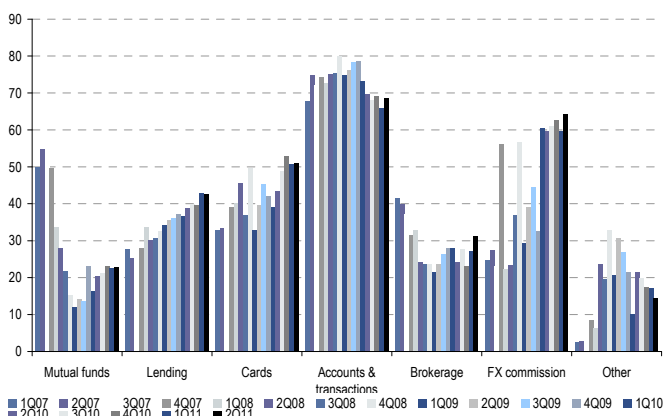
Figure 80. ING BSK – External Net Interest Income by Divisions, 1Q08-1Q11 (Percentage)



Note: Since 1Q11 the bank has disclosed only retail and corporate NII

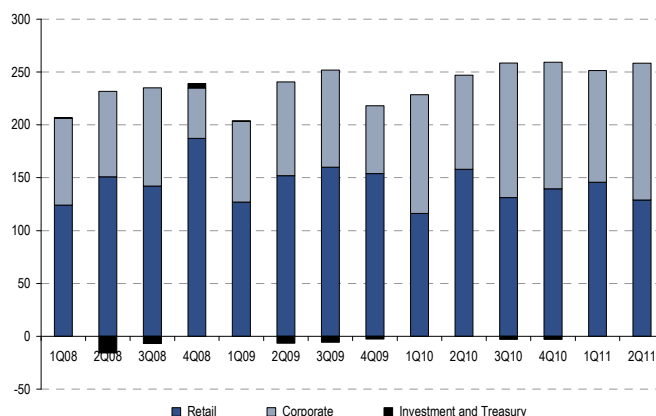
Source: Company reports, Citi Investment Research and Analysis

Figure 81. ING BSK – Breakdown of Fee Income, 1Q07-2Q11 (Polish Zloty in million) corrected



Source: Company reports, Citi Investment Research and Analysis

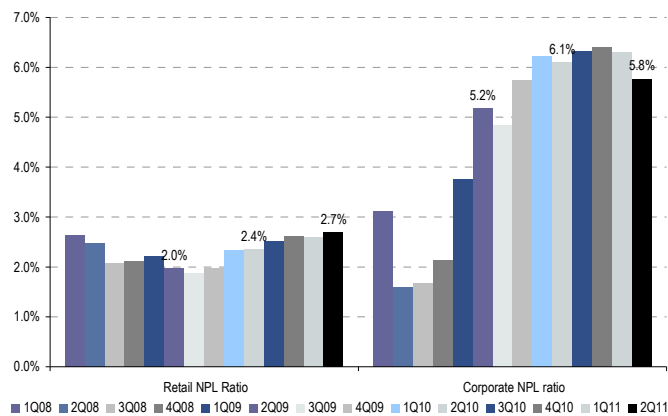
Figure 82. ING BSK – Net Fees by Division, 1Q08-1Q11 (Polish Zloty in million)



Note: Since 1Q11 the bank has disclosed only retail and corporate NII

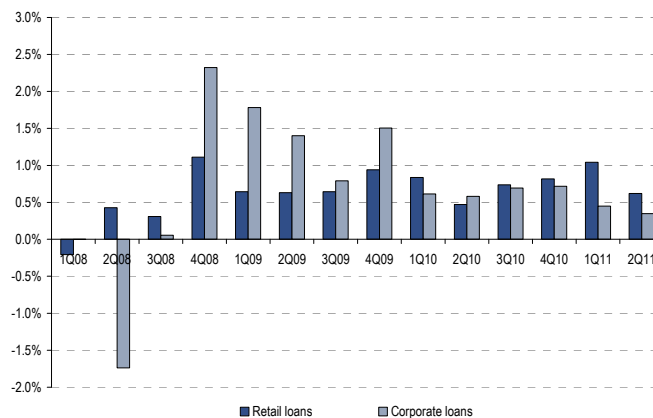
Source: Company reports, Citi Investment Research and Analysis

Figure 83. ING BSK – Retail and Corporate NPL Ratios, 1Q08-1Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 84. ING BSK – Retail and Corporate Cost of Risk, 1Q08-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 85. ING Bank Slaski – Segment Breakdown, 1Q08 – 2Q11 (Polish Zloty in million)

Divisional split (Zl million)	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
NII	262.9	287.7	297.5	303.8	309.5	371.4	391.1	370.1	390.4	405.2	445.1	421.7	434.9	459.5
Retail (*)	129.2	140.7	144.2	115.8	109.3	160.4	159.5	154.4	178.0	202.2	192.3	227.7	245.1	237.7
Corporate (*)	81.6	87.9	93.0	103.7	83.0	91.1	100.3	101.1	212.4	203.1	114.3	123.4	189.8	221.8
Investment and Treasury (*)	52.1	59.1	60.3	84.3	117.2	119.9	131.4	114.5	0.0	0.0	138.6	70.6	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fees	206.7	215.9	228.3	239.1	203.9	234.0	246.2	215.5	228.5	247.0	255.6	256.3	251.4	258.4
Retail	124.2	150.9	142.1	187.1	127.1	152.0	159.9	153.8	116.147	158.098	131.2	139.6	145.7	128.9
Corporate	82.3	80.8	92.9	47.8	76.2	88.6	92.0	64.3	112.321	88.854	127.3	119.7	105.6	129.5
Investment and Treasury	0.2	-15.8	-6.8	4.3	0.7	-6.6	-5.6	-2.6	0	0	-2.9	-3.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0	0	0.0	0.0	0.0	0.0
Total Income	567.5	607.2	602.4	310.2	556.6	670.8	694.0	567.7	654.4	668.1	677.2	679.8	723.2	734.3
Retail	278.9	344.6	323.1	269.7	273.1	337.1	317.3	286.3	307.7	360.0	341.5	372.3	393.8	400.5
Corporate	209.4	202.7	205.7	126.0	125.5	165.5	154.7	154.9	350.5	318.7	228.2	211.9	338.7	350.0
Investment and Treasury	93.2	79.6	80.8	-86.1	158.7	185.2	229.9	144.0	0.0	0.0	130.5	110.5	0.0	0.0
Other	-14.0	-19.8	-7.2	0.6	-0.8	-17.1	-7.9	-17.5	-3.7	-10.6	-23.0	-14.9	-9.3	-16.2
Total costs	-364.4	-385.3	-402.6	-354.6	-361.7	-383.8	-393.0	-349.3	-394.1	-403.5	-395.3	-390.0	-408.7	-419.8
Retail	-234.0	-251.2	-250.1	-228.3	-229.0	-248.0	-252.0	-230.6	-248.5	-256.6	-265.7	-247.3	-250.7	-266.8
Corporate	-116.2	-128.3	-132.3	-107.8	-118.7	-124.7	-126.9	-110.7	-142.1	-146.5	-126.8	-125.2	-157.5	-156.0
Investment and Treasury	-15.1	-10.5	-14.6	-10.6	-14.6	-9.6	-13.5	-11.2	0.0	0.0	-15.2	-20.0	0.0	0.0
Other	0.9	4.8	-5.6	-7.9	0.7	-1.5	-0.7	3.2	-3.6	-0.3	12.3	2.5	-0.5	3.0
Cost/Income	64%	63%	67%	114%	65%	57%	57%	62%	60%	60%	58%	57%	57%	57%
Retail	84%	73%	77%	85%	84%	74%	79%	81%	81%	71%	78%	66%	64%	67%
Corporate	55%	63%	64%	86%	95%	75%	82%	71%	41%	46%	56%	59%	47%	45%
Investment and Treasury	16%	13%	18%	-12%	9%	5%	6%	8%	NA	NA	12%	18%	NA	NA
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Operating income	203.1	221.8	199.8	-44.3	194.9	287.0	300.9	218.4	260.3	264.6	281.9	289.8	314.5	314.5
Retail	44.9	93.4	73.0	41.4	44.1	89.1	65.3	55.7	59.1	103.3	75.8	125.0	143.0	133.7
Corporate	93.2	74.4	73.4	18.3	6.8	40.8	27.8	44.2	208.4	172.2	101.4	86.7	181.2	194.0
Investment and Treasury	78.1	69.1	66.2	-96.7	144.1	175.7	216.5	132.8	0.0	0.0	115.3	90.5	0.0	0.0
Other	-13.1	-15.1	-12.8	-7.3	-0.1	-18.6	-8.6	-14.3	-7.3	-10.9	-10.7	-12.4	-9.7	-13.2
Pre-tax profit	214.3	294.6	205.4	-151.2	102.9	228.7	257.0	149.7	219.5	236.2	237.4	241.0	267.1	290.0
Retail	47.5	87.4	68.1	21.4	31.3	75.6	50.6	32.9	37.9	90.3	54.5	99.4	109.2	112.5
Corporate	93.2	139.0	71.0	-81.2	-72.1	-19.5	-7.0	-23.1	181.6	145.9	67.6	51.1	158.0	177.5
Investment and Treasury	78.1	69.1	63.2	-93.7	144.1	175.7	211.8	138.2	0.0	0.0	115.3	90.5	0.0	0.0
Other	-4.5	-0.8	3.0	2.3	-0.3	-3.0	1.6	1.8	0.0	0.0	0.0	0.0	0.0	0.0

Source: Company Reports, Citi Investment Research and Analysis

Annual Financials

Figure 86. ING BSK – Profit and Loss, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	721	936	29.8%	1,048	11.9%	1,152	9.9%	1,442	25.2%	1,628	12.9%	1,826	12.2%	1,937	6.1%
Net Fee & Commission Income	528	735	39.3%	899	22.2%	890	-1.0%	900	1.1%	987	9.7%	1,037	5.0%	1,110	7.1%
Financial Income	216	80	-62.7%	62	-23.0%	19	-69.8%	147	683.0%	80	-45.6%	81	1.2%	115	42.1%
Other Income	206	19	-90.8%	12	-35.4%	27	119.6%	-10	na	-3	-68.6%	22	na	24	8.4%
Total Revenue	1,670	1,771	6.0%	2,021	14.1%	2,087	3.3%	2,478	18.7%	2,679	8.1%	2,944	9.9%	3,181	8.1%
Labour Costs	-537	-579	7.9%	-700	20.9%	-783	11.7%	-717	-8.4%	-822	14.6%	-852	3.6%	-910	6.9%
General Costs	-445	-503	13.0%	-525	4.5%	-591	12.4%	-647	9.5%	-640	-1.0%	-675	5.5%	-745	10.3%
Depreciation	-128	-142	10.4%	-155	9.3%	-134	-13.6%	-124	-7.4%	-121	-2.4%	-127	5.1%	-133	4.9%
Operating Expenses	-1,109	-1,223	10.3%	-1,381	12.9%	-1,507	9.1%	-1,488	-1.3%	-1,583	6.4%	-1,654	4.5%	-1,789	8.1%
Operating Profit	561	548	-2.4%	640	16.9%	580	-9.3%	991	70.7%	1,097	10.7%	1,290	17.6%	1,393	8.0%
Provision Charge	118	166	40.6%	103	-37.8%	-66	na	-304	364.1%	-204	-33.1%	-226	10.9%	-506	124.2%
Extraordinary Profit/(Loss)	na	na	na	na	na	na	na	na	na	na	na	na	na	na	na
Associate Income	27	40	49.3%	44	9.4%	48	10.6%	52	8.0%	41	-20.8%	36	-12.3%	27	-24.5%
Minorities	-17	-7	-61.2%	-6	-7.6%	0	-99.9%	0	180.0%	0	178.6%	0	317.9%	0	145.4%
Profit Before Tax	706	753	6.7%	787	4.5%	563	-28.5%	738	31.1%	934	26.5%	1,100	17.8%	914	-16.9%
Tax	-139	-155	11.5%	-150	-3.4%	-118	-21.7%	-143	21.8%	-181	26.3%	-214	18.2%	-174	-18.8%
Net Profit	549	591	7.6%	631	6.7%	445	-29.4%	595	33.6%	753	26.6%	886	17.7%	740	-16.5%
EPS (Zl)	42.2	45.5	7.6%	48.5	6.7%	34.2	-29.4%	45.7	33.6%	57.9	26.6%	68.1	17.7%	56.9	-16.5%
DPS (Zl)	27.5	27.9	1.5%	11.7	-58.1%	0.0	na	0.0	na	15.0	na	13.6	-9.2%	34.1	150.5%
Average Diluted Number of Shares (m)	13.0	13.0	0.0%	13.0	0.0%	13.0	0.0%	13.0	0.0%	13.0	0.0%	13.0	0.0%	13.0	0.0%

Source: Company reports, CIRA estimates

Figure 87. ING BSK – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Cash and NBP Balances	1,176	1,148	-2.4%	1,842	60.4%	1,370	-25.6%	2,657	93.9%	2,394	-9.9%	2,586	8.0%	2,793	8.0%
Interbank placements	12,574	13,514	7.5%	15,184	12.4%	7,787	-48.7%	1,184	-84.8%	1,181	-0.3%	1,205	2.0%	1,229	2.0%
Financial Assets & Securities	17,078	19,686	15.3%	17,300	-12.1%	33,377	92.9%	24,091	-27.8%	24,930	3.5%	25,716	3.2%	26,684	3.8%
Net client lending	9,903	12,868	29.9%	16,379	27.3%	25,743	57.2%	30,593	18.8%	34,509	12.8%	40,118	16.3%	44,283	10.4%
Fixed assets	601	571	-5.0%	533	-6.7%	544	2.1%	549	0.9%	544	-0.8%	577	6.0%	611	6.0%
Other assets	795	689	-13.3%	773	12.1%	790	2.2%	810	2.5%	959	18.4%	956	-0.4%	976	2.2%
Total Assets	42,127	48,476	15.1%	52,011	7.3%	69,610	33.8%	59,883	-14.0%	64,518	7.7%	71,157	10.3%	76,576	7.6%
Interbank borrowing	1,329	2,097	57.8%	1,810	-13.7%	11,993	562.5%	3,974	-66.9%	4,039	1.6%	5,655	40.0%	5,937	5.0%
Client deposits	32,824	38,561	17.5%	44,502	15.4%	47,067	5.8%	47,585	1.1%	47,400	-0.4%	50,729	7.0%	54,373	7.2%
Other liabilities	4,413	4,039	-8.5%	1,858	-54.0%	6,326	240.4%	3,438	-45.6%	7,425	116.0%	8,379	12.8%	9,308	11.1%
Minorities	12	23	82.3%	2	-92.4%	2	33.7%	2	0.6%	2	1.7%	2	5.2%	3	16.2%
Equity (ex Minorities)	3,549	3,756	5.8%	3,839	2.2%	4,222	10.0%	4,884	15.7%	5,651	15.7%	6,391	13.1%	6,954	8.8%
Total liabilities & Equity	42,127	48,476	15.1%	52,011	7.3%	69,610	33.8%	59,883	-14.0%	64,518	7.7%	71,157	10.3%	76,576	7.6%
Interest Earning Assets	40,731	47,216	15.9%	50,705	7.4%	68,276	34.7%	58,525	-14.3%	63,014	7.7%	69,625	10.5%	74,988	7.7%
BVPS (Zl)	273	289	5.8%	295	2.2%	325	10.0%	375	15.7%	434	15.7%	491	13.1%	535	8.8%

Source: Company reports, CIRA estimates

Figure 88. ING BSK – Key Ratios, 2005-2012E (Percentage)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	1.93%	2.13%	2.14%	1.94%	2.27%	2.68%	2.75%	2.68%
NIM on Total Ave. Assets	1.86%	2.07%	2.09%	1.89%	2.23%	2.62%	2.69%	2.62%
Net Fee & Commission Income/Total Income	31.6%	41.5%	44.5%	42.6%	36.3%	36.8%	35.2%	34.9%
Net Fee & Commission Income/Deposits	1.3%	1.6%	2.0%	1.9%	1.9%	2.1%	2.0%	2.0%
Cost/Income	66.4%	69.1%	68.3%	72.2%	60.0%	59.1%	56.2%	56.2%
Cost/Avg. Assets	2.9%	2.7%	2.7%	2.5%	2.3%	2.5%	2.4%	2.4%
Effective tax rate	19.7%	20.6%	19.1%	20.9%	19.4%	19.4%	19.4%	19.0%
Dividend Payout Ratio	65.1%	61.4%	24.1%	0.0%	0.0%	25.9%	20.0%	60.0%
Provisions/Avg Net Loans	-1.16%	-1.46%	-0.71%	0.31%	1.08%	0.63%	0.60%	1.20%
Equity/Assets	8.5%	7.8%	7.4%	6.1%	8.2%	8.8%	9.0%	9.1%
Loans/Deposits	35.8%	39.2%	36.8%	54.7%	64.3%	72.8%	79.1%	81.4%
Loans/Total Assets	23.5%	26.5%	31.5%	37.0%	51.1%	53.5%	56.4%	57.8%
ROE	16.4%	16.2%	16.6%	11.1%	13.1%	14.3%	14.7%	11.1%
ROA	1.42%	1.31%	1.26%	0.73%	0.92%	1.21%	1.31%	1.00%
NPLs/Total Loans	8.2%	5.1%	3.0%	1.9%	3.7%	4.2%	4.5%	4.5%
Provision Coverage of NPLs	91.3%	102.1%	110.8%	100.0%	75.7%	72.0%	67.6%	83.2%
RWA/Total Assets	36.3%	39.2%	43.7%	52.7%	58.2%	57.1%	63.0%	63.0%
CAR	18.6%	15.7%	13.1%	10.4%	12.0%	13.1%	12.5%	12.7%
Group Employees	7,446	7,515	8,074	8,577	8,291	8,472	8,502	8,502

Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Hold/Medium Risk	2M
Price (29 Sep 11)	ZL224.00
Target price	ZL239.00
from ZL253.00	
Expected share price return	6.7%
Expected dividend yield	4.4%
Expected total return	11.1%
Market Cap	ZL16,369M
	US\$4,987M

Price Performance (RIC: BZWB.WA, BB: BZW PW)



Bank Zachodni WBK (BZWB.WA) Waiting For 'Santanderisation': Maintaining Hold

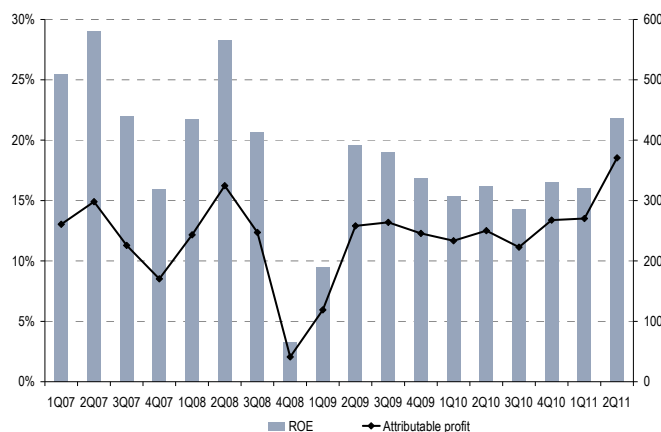
- **Retail Driven by Higher NII and Lower Provisioning** — In line with sector trends, the 2Q11 profitability of BZ WBK's retail division (pre-tax of ZL 170m, +386% yoy, +17% qoq) was driven by higher NII (+22% yoy, +7% qoq) and lower provisioning (-56% yoy, -16% qoq) as well as 9% yoy growth in non-interest income.
- **Low Cost of Risk in Corporate Division Continued** — Due to continued low cost of risk (38bp vs. 44bp in 1Q11 and 37bp in 2Q10), the corporate division continued to post solid pre-tax profit (ZL 101m, -4% yoy, -12% qoq) but its profitability was negatively affected by rising administrative costs (+13% yoy).
- **As Good As Usual** — We appreciate the high quality of BZ WBK's management and strategy and see no material risk of problems with either as a result of the entry of Santander (although the long process of appointing a new CFO after the resignation of Mr. Paul Barry was disappointing). We like BZ WBK's plans to increase lending to SMEs and restructure its investment fund business and wait for the first signs of co-operation with Santander in credit cards, bancassurance, and Corporate and Investment Banking (CIB) to become visible.
- **M&A Opportunity** — According to the *Gazeta Wyborcza* daily, Santander has just completed due diligence in Kredyt Bank and has made an offer for the bank. KBC is expected to respond soon; if it doesn't accept the offer it will start a regular tender, according to the report. The companies in question have not commented on the report. Were Kredyt Bank acquired inexpensively (which, in our view, given the low quality of the business, might be the case in the absence of an open tender) by Santander, it would create the third-biggest bank in Poland in every category while cost synergy potential would be material, in our view.
- **2012E EPS Cut by 19%** — We reduce our NIM estimate to 3.47% from 3.62% in 2012 and to 3.47% from 3.60% in 2013, lower our loan growth forecasts to 8% from 15% in 2012 and to 8% from 13% in 2013 and increase our cost of risk to 130p from 79bp (in both years). These changes lead us to cut our EPS estimates by 19% and 21%, respectively.
- **Maintaining Hold** — We maintain our assumption of a sustainable ROE of 18.0% but due to lowered 2012 and 2013 EPS estimates we reduce our target price to ZL 239 from ZL 253. We maintain our Hold/Medium Risk (2M) rating.

Bank Zachodni WBK (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	886.2	974.2	1,218.2	1,078.8	1,186.5
Diluted EPS (ZL)	12.05	13.25	16.57	14.67	16.14
Diluted EPS (Old) (ZL)	12.05	13.25	16.72	18.17	20.46
PE (x)	18.6	16.9	13.5	15.3	13.9
P/BV (x)	2.8	2.5	2.3	2.1	2.0
DPS (ZL)	4.00	8.00	9.95	8.81	12.92
Net Div Yield (%)	1.8	3.6	4.4	3.9	5.8
ROE (%)	16.2	15.5	17.5	14.4	15.0

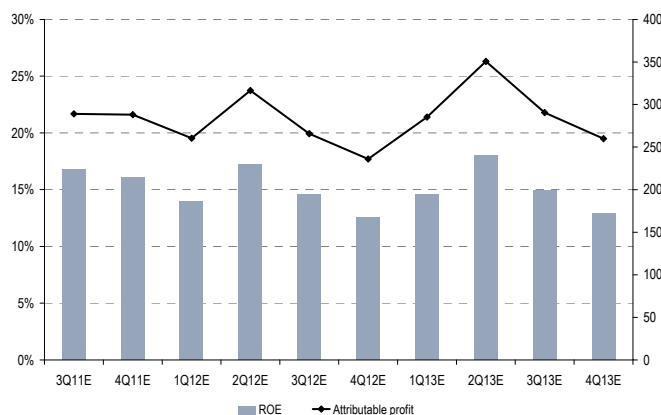
BZ WBK in Snapshots

Figure 89. BZ WBK – Reported Net Profit and ROE, 1Q07-2Q11 (Polish Zloty in million/Percentage)



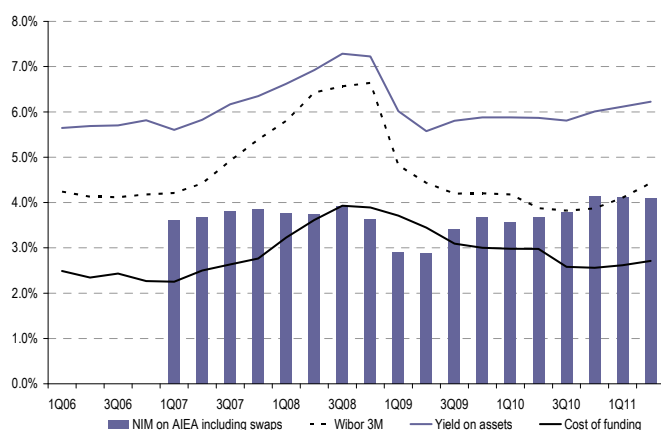
Source: Company reports, Citi Investment Research and Analysis

Figure 90. BZ WBK – Forecast Net Profit and ROE, 3Q11E-4Q13E (Polish Zloty in million/Percentage)



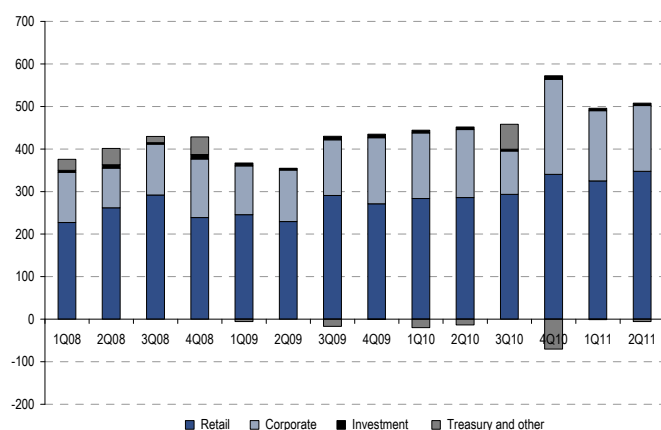
Source: Citi Investment Research and Analysis

Figure 91. BZ WBK – Yield on Assets and Cost of Funding, 1Q06-2Q11 (Percentage)



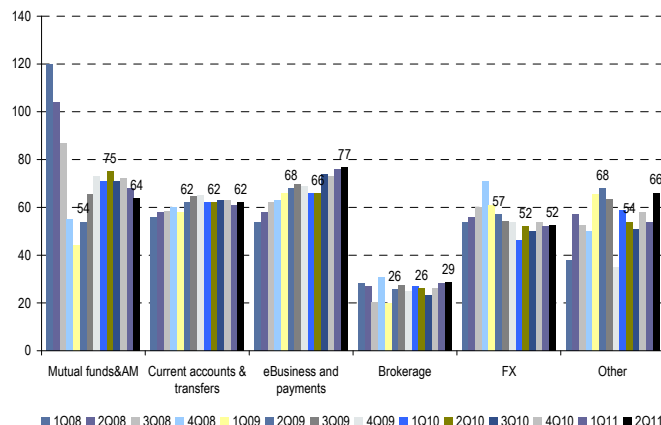
Source: Company reports, Citi Investment Research and Analysis

Figure 92. BZ WBK – Net Interest Income by Divisions, 1Q08-2Q11 (Percentage)



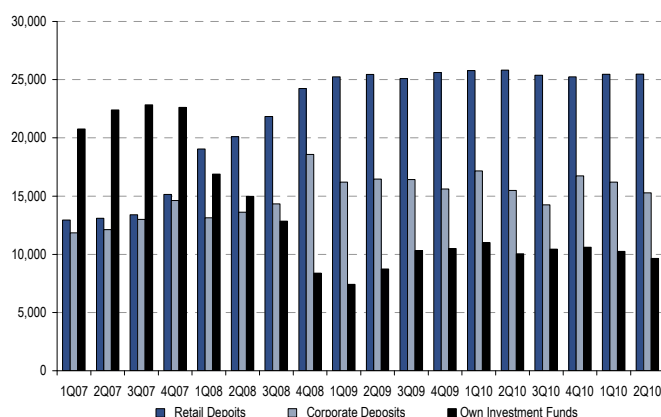
Source: Company reports, Citi Investment Research and Analysis

Figure 93. BZ WBK – Breakdown of Fee Income, 1Q08-2Q11 (Polish Zloty in million)



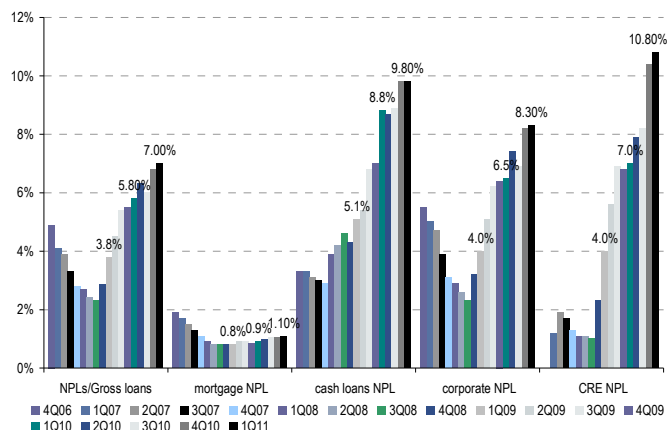
Source: Company reports, Citi Investment Research and Analysis

Figure 94. BZ WBK – Deposits and Investment Fund AuM, 1Q07-2Q11 (Polish Zloty in million)



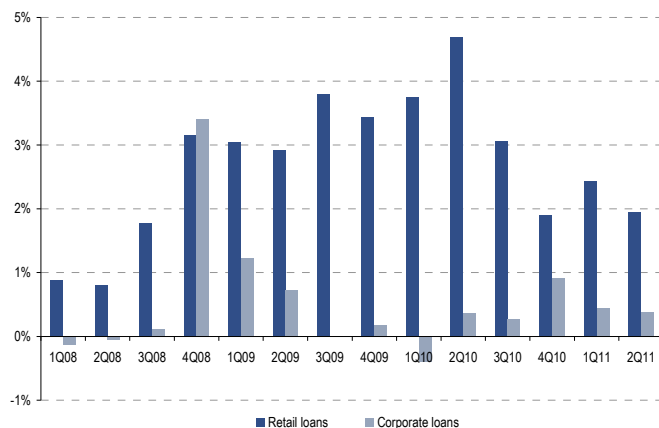
Source: Company reports, Citi Investment Research and Analysis

Figure 95. BZ WBK – Retail and Corporate NPL Ratios, 4Q06-1Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 96. BZ WBK – Retail and Corporate Cost of Risk, 1Q08-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 97. BZ WBK – Segment Breakdown, 1Q08–2Q11 (Polish Zloty in million)

	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Nil	375.7	401.4	429.5	428.5	361.5	354.9	412.9	433.8	424.5	438.3	457.9	501.5	494.6	502.5
Retail	226.9	261.8	291.9	238.9	245.7	229.6	290.6	271.2	283.6	285.9	293.3	340.6	325.1	347.6
Corporate	118.4	93.4	119.3	137.8	114.5	121.0	131.1	155.0	154.4	159.7	101.6	223.0	165.1	154.2
Investment	4.5	7.9	3.9	10.0	6.6	3.2	8.3	8.3	6.0	5.8	4.5	8.1	5.4	6.2
Treasury and other	26.0	38.3	14.5	41.8	-5.3	1.2	-17.1	-0.7	-19.5	-13.2	58.5	-70.3	-1.0	-5.4
Total Income	759.7	893.4	818.6	786.2	738.8	853.1	826.7	870.5	840.2	909.8	858.6	931.2	890.4	1,011.2
Retail	411.7	476.3	514.5	444.1	455.4	443.4	509.7	460.9	491.2	497.6	505.4	559.0	545.4	579.3
Corporate	148.5	114.7	139.2	149.3	130.5	147.0	152.4	177.9	175.6	179.4	130.5	248.7	196.8	181.9
Investment	132.4	219.2	97.4	132.5	64.8	156.0	86.6	118.0	94.0	147.5	84.9	96.4	85.6	154.6
Treasury and other	67.1	83.2	67.5	60.3	88.1	106.8	78.0	113.7	79.4	85.3	137.8	27.1	62.6	95.3
Total costs	-405.2	-440.1	-431.5	-405.3	-413.6	-403.8	-388.6	-438.8	-421.5	-431.1	-451.2	-462.5	-445.2	-465.3
Retail	-284.2	-326.4	-310.8	-342.2	-300.8	-305.8	-294.7	-319.1	-311.7	-332.1	-331.7	-318.9	-332.4	-351.9
Corporate	-52.3	-51.5	-48.5	-45.5	-56.9	-48.0	-48.8	-43.5	-50.9	-51.5	-52.7	-55.9	-57.1	-58.4
Investment	-45.3	-47.2	-44.4	-35.6	-33.6	-38.3	-38.0	-40.4	-38.6	-39.9	-39.0	-43.7	-40.8	-36.7
Treasury and other	-23.4	-15.0	-27.9	18.0	-22.3	-11.7	-7.1	-35.8	-20.3	-7.5	-27.9	-44.0	-15.0	-18.4
Cost/Income	53%	49%	53%	52%	56%	47%	47%	50%	50%	47%	53%	50%	50%	46%
Retail	69%	69%	60%	77%	66%	69%	58%	69%	63%	67%	66%	57%	61%	61%
Corporate	35%	45%	35%	30%	44%	33%	32%	24%	29%	29%	40%	22%	29%	32%
Investment	34%	22%	46%	27%	52%	25%	44%	34%	41%	27%	46%	45%	48%	24%
Treasury and other	35%	18%	41%	-30%	25%	11%	9%	31%	26%	9%	20%	162%	24%	19%
Operating income	354.6	453.3	387.1	380.9	325.3	449.3	438.2	431.6	418.7	478.7	407.4	468.7	445.1	545.8
Retail	127.5	149.9	203.7	101.9	154.6	137.6	215.1	141.8	179.5	165.5	173.7	240.1	212.9	227.4
Corporate	96.2	63.2	90.7	103.8	73.6	98.9	103.6	134.4	124.7	127.9	77.8	192.8	139.8	123.6
Investment	87.2	172.0	53.0	96.9	31.2	117.7	48.6	77.6	55.4	107.5	46.0	52.7	44.8	117.9
Treasury and other	43.7	68.2	39.6	78.3	65.8	95.1	70.9	77.9	59.1	77.8	110.0	-16.9	47.7	76.9
Pre-tax profit	348.5	439.5	342.1	80.4	161.6	326.0	343.9	331.4	348.1	333.8	307.9	367.4	353.5	468.8
Retail	113.0	134.9	165.1	29.4	77.4	64.1	119.3	50.3	78.5	35.1	86.9	187.2	145.2	170.5
Corporate	103.0	66.1	83.6	-124.1	-12.9	49.2	104.7	123.3	148.7	105.1	61.8	140.4	114.3	100.8
Investment	87.1	172.1	53.9	96.7	31.2	117.7	49.1	79.9	55.4	107.6	47.6	52.8	45.6	118.0
Treasury and other	45.4	66.4	39.5	78.4	65.8	95.1	70.9	77.9	65.5	85.9	111.7	-13.0	48.3	79.6

Source: Company reports

Annual Financials

Figure 98. BZ WBK – Profit and Loss, 2005-2012E (Polish Zloty in million)

	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	909	1,032	13.5%	1,287	24.7%	1,635	27.1%	1,563	-4.4%	1,822	16.6%	2,018	10.8%	2,033	0.7%
Net Fee & Commission Income	694	1,191	71.6%	1,545	29.7%	1,390	-10.1%	1,315	-5.3%	1,345	2.2%	1,423	5.8%	1,558	9.5%
Financial Income	24	85	259.4%	44	-48.0%	95	114.8%	264	178.4%	271	2.6%	240	-11.6%	261	8.9%
Other Income	288	66	-77.1%	79	19.6%	111	40.7%	123	11.4%	65	-47.4%	106	63.4%	95	-10.4%
Total Revenue	1,915	2,374	24.0%	2,955	24.5%	3,230	9.3%	3,266	1.1%	3,503	7.2%	3,787	8.1%	3,947	4.2%
Labour Costs	-574	-684	19.0%	-843	23.3%	-896	6.4%	-889	-0.8%	-959	7.8%	-998	4.1%	-1,049	5.1%
General Costs	-404	-447	10.7%	-582	30.1%	-651	11.8%	-609	-6.4%	-642	5.4%	-703	9.6%	-773	9.9%
Depreciation	-186	-159	-14.8%	-135	-15.2%	-107	-20.3%	-123	15.0%	-129	4.3%	-144	11.9%	-149	3.7%
Operating Expenses	-1,165	-1,290	10.7%	-1,559	20.9%	-1,655	6.1%	-1,622	-2.0%	-1,729	6.6%	-1,846	6.7%	-1,972	6.8%
Operating Profit	750	1,084	44.6%	1,395	28.7%	1,576	12.9%	1,644	4.3%	1,773	7.9%	1,942	9.5%	1,975	1.7%
Provision Charge	-62	-28	-54.0%	-4	-86.1%	-365	9162%	-481	32.0%	-421	-12.5%	-348	-17.2%	-503	44.3%
Associate Income	0	10	1970%	0	-98.0%	-1	na	0	-57.0%	4	na	7	54.9%	4	-42.0%
Profit Before Tax	689	1,065	54.7%	1,391	30.6%	1,211	-13.0%	1,163	-3.9%	1,357	16.7%	1,600	17.9%	1,476	-7.8%
Minorities	-30	-86	190.7%	-156	81.3%	-99	-36.6%	-54	-45.4%	-66	22.9%	-68	2.2%	-99	45.7%
Tax	-144	-221	54.1%	-281	26.9%	-256	-8.7%	-223	-13.1%	-317	42.1%	-314	-0.8%	-298	-5.0%
Net Profit	516	758	47.1%	955	25.9%	855	-10.4%	886	3.6%	974	9.9%	1,218	25.0%	1,079	-11.4%
EPS (Zl)	7.1	10.4	46.9%	13.1	25.8%	11.7	-10.7%	12.1	3.3%	13.2	9.9%	16.6	25.0%	14.7	-11.4%
DPS (Zl)	6.00	6.00	0.1%	3.00	-50.0%	0.00	na	4.00	na	8.00	100.0%	9.95	24.4%	8.81	-11.4%
Average Diluted Number of Shares (m)	73.0	73.0	0.1%	73.1	0.1%	73.3	0.3%	73.5	0.3%	73.5	0.0%	73.5	0.0%	73.5	0.0%

Source: Company reports, CIRA estimates

Figure 99. BZ WBK – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Cash and NBP Balances	572	1,534	168.1%	2,206	43.8%	3,178	44.0%	2,661	-16.3%	2,534	-4.7%	2,815	11.1%	3,128	11.1%
Interbank placements	3,624	3,155	-12.9%	2,577	-18.3%	1,365	-47.0%	663	-51.4%	620	-6.5%	688	11.1%	765	11.1%
Financial Assets & Securities	9,651	9,146	-5.2%	11,063	21.0%	16,141	45.9%	14,646	-9.3%	15,649	6.8%	16,008	2.3%	16,412	2.5%
Net client lending	14,194	17,620	24.1%	23,950	35.9%	35,137	46.7%	34,571	-1.6%	32,838	-5.0%	37,165	13.2%	40,229	8.2%
Fixed assets	519	494	-4.8%	543	10.0%	637	17.4%	596	-6.5%	548	-8.2%	608	11.1%	676	11.1%
Other assets	1,041	1,044	0.2%	993	-4.9%	974	-1.8%	922	-5.4%	965	4.7%	1,035	7.3%	1,080	4.3%
Total Assets	29,601	32,992	11.5%	41,332	25.3%	57,433	39.0%	54,058	-5.9%	53,154	-1.7%	58,321	9.7%	62,288	6.8%
Interbank borrowing	2,692	2,608	-3.1%	4,484	71.9%	5,338	19.1%	5,350	0.2%	2,526	-52.8%	6,315	150.0%	6,252	-1.0%
Client deposits	20,839	24,222	16.2%	29,766	22.9%	42,811	43.8%	41,223	-3.7%	41,970	1.8%	42,417	1.1%	45,913	8.2%
Other liabilities	2,260	2,085	-7.8%	2,506	20.2%	4,072	62.5%	1,430	-64.9%	1,884	31.7%	2,125	12.8%	2,212	4.1%
Minorities	55	117	112.5%	235	101.4%	240	2.0%	108	-54.8%	151	38.9%	152	0.9%	251	65.0%
Equity (ex Minorities)	3,755	3,960	5.5%	4,342	9.6%	4,973	14.5%	5,947	19.6%	6,623	11.4%	7,312	10.4%	7,660	4.8%
Total liabilities & Equity	29,601	32,992	11.5%	41,332	25.3%	57,433	39.0%	54,058	-5.9%	53,154	-1.7%	58,321	9.7%	62,288	6.8%
BVPS (Zl)	51	54	5.5%	60	9.6%	68	14.5%	81	19.4%	91	11.4%	100	9.8%	104	4.8%

Source: Company reports, CIRA estimates

Figure 100. BZ WBK – Key Ratios, 2005-2012E (Percentage)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	3.37%	3.47%	3.61%	3.42%	2.89%	3.47%	3.70%	3.47%
NIM on Total Ave. Assets	3.18%	3.30%	3.46%	3.31%	2.80%	3.40%	3.62%	3.37%
Net Fee & Commission Income/Total Income	36.3%	50.2%	52.3%	43.0%	40.3%	38.4%	37.6%	39.5%
Net Fee & Commission Income/Deposits	3.3%	4.9%	5.2%	3.2%	3.2%	3.2%	3.4%	3.4%
Cost/Income	60.8%	54.3%	52.8%	51.2%	49.7%	49.4%	48.7%	50.0%
Cost/Avg. Assets	4.1%	4.1%	4.2%	3.4%	2.9%	3.2%	3.3%	3.3%
Effective tax rate	20.8%	20.8%	20.2%	21.2%	19.2%	23.3%	19.6%	20.2%
Dividend Payout Ratio	84.9%	57.8%	22.9%	0.0%	33.0%	60.0%	60.0%	60.0%
Provisions/Avg Net Loans	0.44%	0.18%	0.02%	1.23%	1.38%	1.25%	1.00%	1.30%
Equity/Assets	12.9%	12.4%	11.1%	9.1%	11.2%	12.7%	12.8%	12.7%
Loans/Deposits	68.1%	72.7%	80.5%	82.1%	83.9%	78.2%	87.6%	87.6%
Loans/Total Assets	48.0%	53.4%	57.9%	61.2%	64.0%	61.8%	63.7%	64.6%
ROE	14.3%	19.7%	23.0%	18.4%	16.2%	15.5%	17.5%	14.4%
ROA	1.80%	2.42%	2.57%	1.73%	1.59%	1.82%	2.19%	1.79%
NPLs/Total Loans	6.9%	4.9%	2.8%	2.9%	5.5%	6.8%	6.6%	6.0%
Provision Coverage of NPLs	70.6%	72.2%	85.2%	85.7%	58.2%	58.6%	58.3%	69.3%
RWA/Total Assets	57.0%	67.1%	68.9%	76.9%	77.1%	74.5%	76.0%	76.0%
CAR	16.0%	15.5%	13.3%	10.7%	13.0%	15.8%	15.7%	15.4%
Group Employees	7,645	7,946	9,086	10,221	9,453	9,840	9,744	9,841

Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Sell/Medium Risk	3M
Price (29 Sep 11)	ZL4.61
Target price	ZL4.53
from ZL5.00	
Expected share price return	-1.7%
Expected dividend yield	3.3%
Expected total return	1.5%
Market Cap	ZL5,592M
	US\$1,704M

Price Performance (RIC: BIGW.WA, BB: MIL PW)



Bank Millennium SA (BIGW.WA)

Retail Franchise Under Review: Maintaining Sell

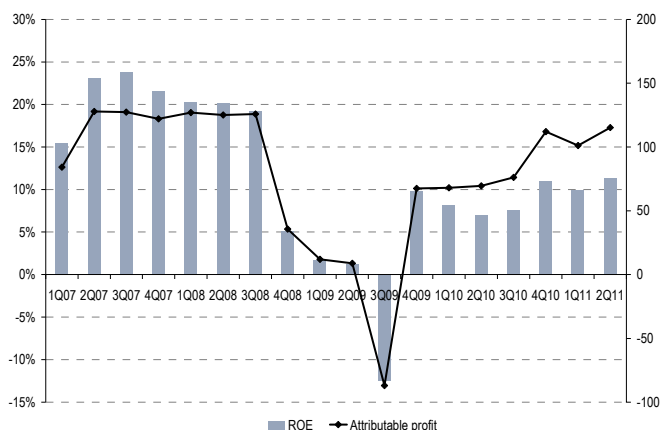
- **Strong Retail Division** — In 2Q11, the retail division continued to be the main driver of the bank's results (pre-tax profit of ZL 151m, +244% yoy and +12% qoq), positively affected by increased net interest income (+33% yoy, +13% qoq) and low cost of risk (31bp vs. 32bp in 1Q11 and 33bp in 2Q10).
- **...vs. Weak Corporate & Treasury Division** — The profitability of the corporate division (pre-tax profit of ZL 29m, +44% yoy, -16% qoq), although positively influenced by higher NII, continued to be negatively impacted by high cost of risk (97bp vs. 68bp in 1Q11 and 117bp in 2Q11). The treasury division again posted a loss in 2Q11 (pre-tax ZL -33m vs. ZL -41m in 1Q11 and ZL 23m in 2Q10).
- **Attractive Retail Franchise** — The sixth-biggest branch network, strong brand awareness, a sizable client base and a low-risk business model make Millennium's retail division attractive, in our view. Given these factors, we are not surprised that the bank's sale has attracted interest (BCP has confirmed it has received 3 written offers and a few additional verbal signs of interest; the *Gazeta Wyborcza* daily speculated that the offers were placed by PKO BP, Pekao and BNP, although none of the companies has commented). Given such levels of interest, we think the bank could be sold at a premium to the market price. Still, due to the risk that minority investors will not be able to sell their shares at the same price, we continue to value Bank Millennium on a standalone basis.
- **2012E EPS Cut by 49%** — We reduce our NIM estimates to 2.04% from 2.45% in 2012 and to 2.04% from 2.35% in 2013, lower our loan growth forecast to 7% from 13% (in both years) and increase our cost of risk to 100bp from 57bp in 2012 and to 100bp from 50bp in 2013. These changes lead us to cut our EPS estimates by 49% and 47%, respectively.
- **Maintaining Sell** — We maintain our assumption of sustainable ROE of 13.5% but due to lowered 2012 and 2013 EPS estimates we decrease our target price to ZL 4.53 from ZL 5.00. We maintain our Sell/Medium Risk (3M) rating.

Bank Millennium SA (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	1.5	326.0	462.0	291.6	359.5
Diluted EPS (ZL)	0.00	0.30	0.38	0.24	0.30
Diluted EPS (Old) (ZL)	0.00	0.30	0.39	0.47	0.55
PE (x)	2,977.7	15.4	12.1	19.2	15.6
P/BV (x)	1.6	1.4	1.3	1.2	1.2
DPS (ZL)	0.00	0.10	0.15	0.12	0.15
Net Div Yield (%)	0.0	2.2	3.3	2.6	3.2
ROE (%)	0.1	9.5	10.9	6.6	7.8

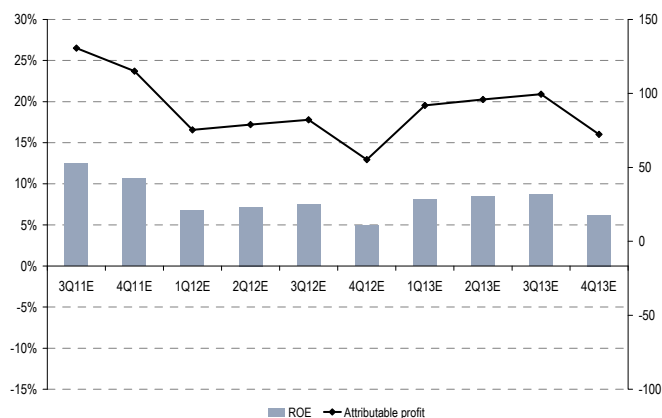
Bank Millennium in Snapshots

Figure 101. Bank Millennium – Reported Net Profit and ROE, 1Q07-2Q11 (Polish Zloty in million/Percentage)



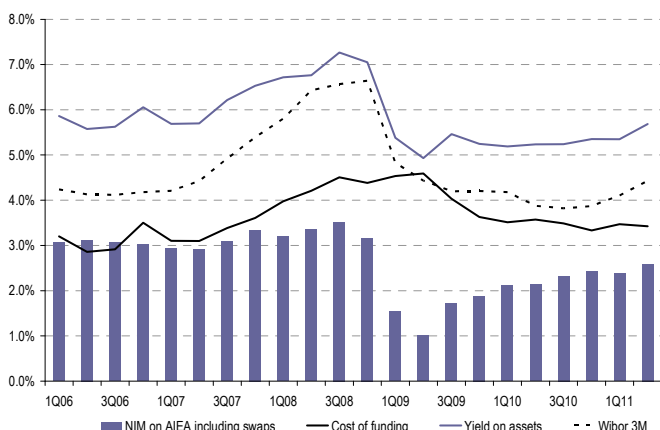
Source: Company reports, Citi Investment Research and Analysis

Figure 102. Bank Millennium – Forecast Net Profit and ROE, 3Q11E-4Q13E (Polish Zloty in million/Percentage)



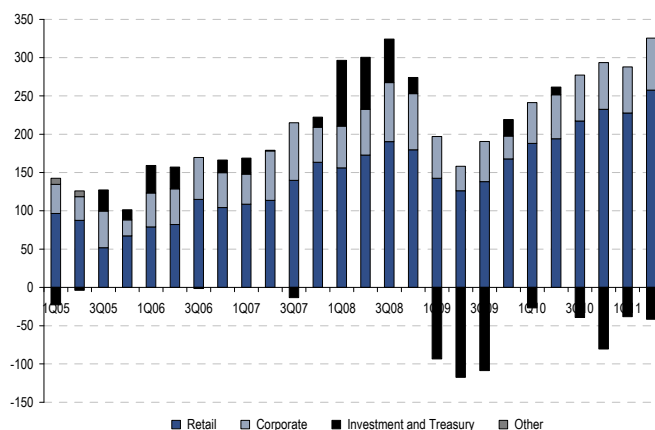
Source: Citi Investment Research and Analysis

Figure 103. Bank Millennium – Yield on Assets and Cost of Funding, 1Q06-2Q11 (Percentage)



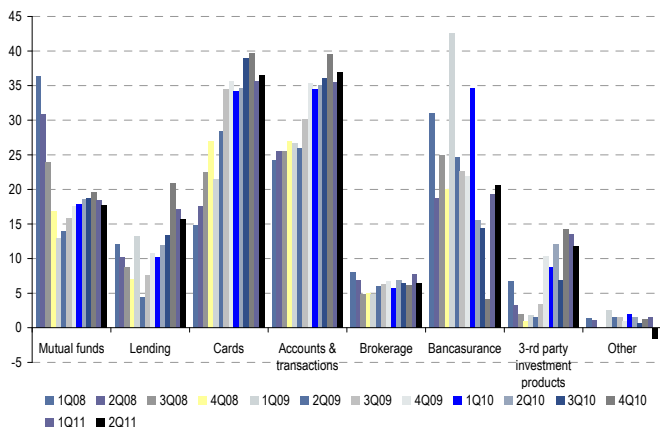
Source: Company reports, Citi Investment Research and Analysis

Figure 104. Bank Millennium – Net Interest Income by Divisions, 1Q05-2Q11 (Polish Zloty in million)



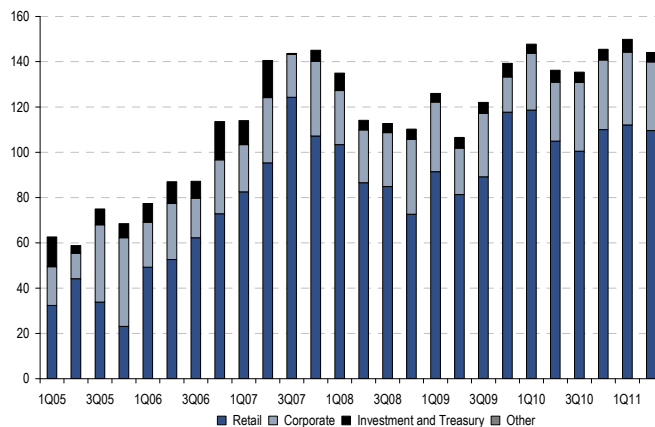
Source: Company reports, Citi Investment Research and Analysis

Figure 105. Bank Millennium – Breakdown of Fee Income, 1Q08-2Q11 (Polish Zloty in million)



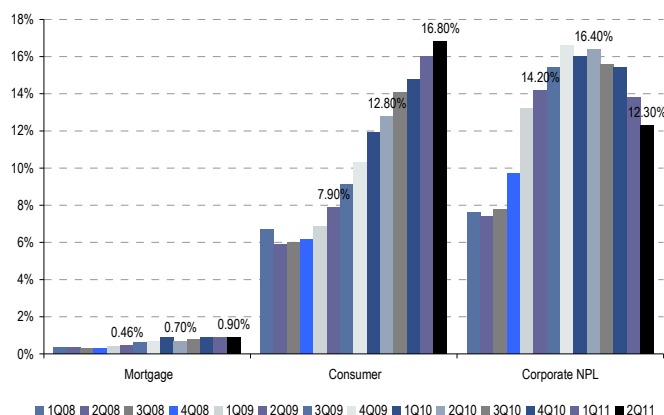
Source: Company reports, Citi Investment Research and Analysis

Figure 106. Bank Millennium – Net Fees by Divisions, 1Q05-2Q11 (Polish Zloty in million)



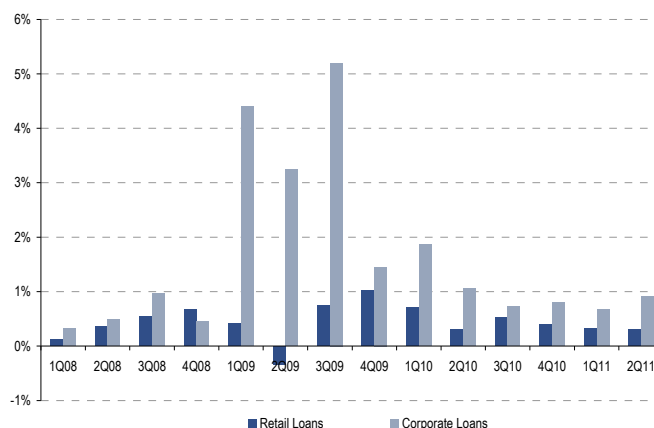
Source: Company reports, Citi Investment Research and Analysis

Figure 107. Bank Millennium – Mortgage, Consumer and Corporate NPL Ratios, 1Q08-2Q11 (Percentage)



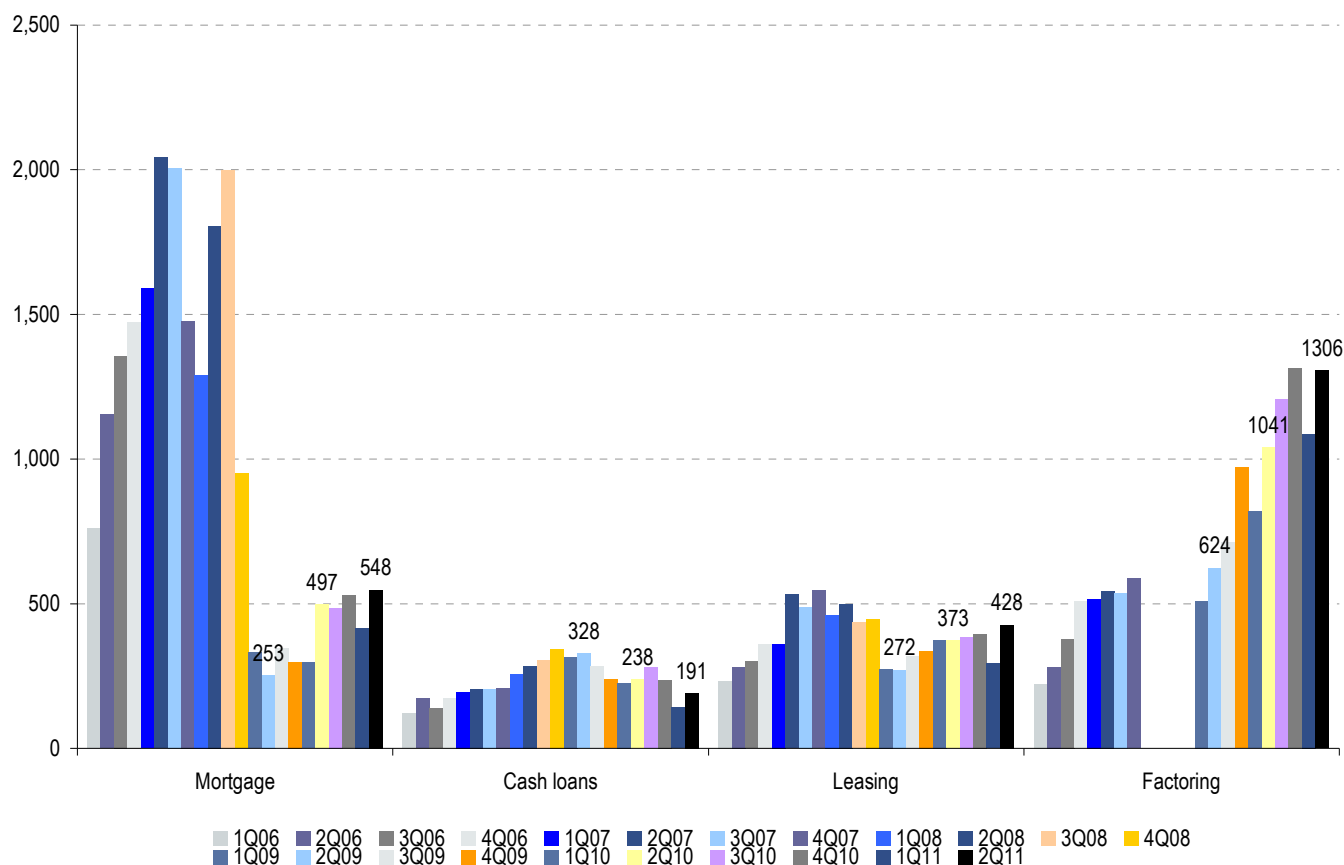
Source: Company reports, Citi Investment Research and Analysis

Figure 108. Bank Millennium – Retail and Corporate Cost of Risk, 1Q08-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 109. Bank Millennium – Quarterly Production, 1Q06-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 110. Bank Millennium – Segment Breakdown, 1Q07–2Q11 (Polish Zloty in million)

	1Q07	2Q07	3Q07	4Q07	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Nil	169	179	202	222	223	238	251	269	128	85	190	196	217	218	239	253	256	288
Retail	109	114	140	163	156	173	190	180	142	126	138	168	188	194	217	232	228	258
Corporate	39	65	75	46	55	60	77	73	55	32	53	30	53	58	60	61	60	68
Investment and Treasury	21	1	-13	13	86	68	57	21	-93	-118	-109	21	-27	10	-39	-80	-38	-41
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Fees	114	141	144	145	135	114	113	110	126	107	122	139	148	136	135	145	150	144
Retail	82	95	124	107	103	87	85	73	91	81	89	118	119	105	100	110	112	110
Corporate	21	29	19	33	24	23	24	33	31	20	28	16	25	26	30	31	32	30
Investment and Treasury	11	16	0	5	8	4	4	5	4	5	5	6	4	5	5	5	6	4
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Income	371	427	448	464	445	485	505	413	400	320	316	417	423	403	418	472	439	473
Retail	231	255	307	314	302	317	343	321	260	230	247	308	326	266	336	416	364	385
Corporate	76	112	114	105	99	112	137	-13	120	58	90	29	86	94	99	106	100	104
Investment and Treasury	63	59	27	45	45	56	25	105	20	32	-21	80	11	43	-17	-54	-24	-17
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	0	0
Total costs	-231	-248	-270	-308	-275	-299	-303	-313	-257	-262	-262	-241	-255	-269	-274	-284	-273	-282
Retail	-165	-179	-202	-216	-211	-205	-233	-237	-195	-198	-199	-184	-195	-201	-207	-210	-206	-212
Corporate	-49	-54	-51	-74	-52	-54	-64	-76	-49	-48	-46	-41	-44	-50	-52	-57	-50	-53
Investment and Treasury	-17	-15	-17	-18	-11	-40	-6	0	-14	-16	-18	-16	-16	-18	-15	-17	-16	-17
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Cost/Income	62%	58%	60%	66%	62%	62%	60%	76%	64%	82%	83%	58%	60%	67%	66%	60%	62%	60%
Retail	72%	70%	66%	69%	70%	64%	68%	74%	75%	86%	80%	60%	60%	76%	62%	50%	57%	55%
Corporate	64%	48%	45%	71%	53%	49%	47%	-598%	40%	82%	51%	142%	51%	53%	53%	54%	50%	51%
Investment and Treasury	26%	25%	61%	40%	25%	72%	24%	0%	69%	51%	-85%	20%	140%	43%	-86%	-31%	-68%	-99%
Other	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Operating income	140	179	178	156	170	186	202	100	143	58	54	176	169	134	144	188	167	191
Retail	65	76	104	98	90	113	110	83	65	32	49	125	131	65	129	206	158	173
Corporate	28	58	63	31	46	58	73	-89	72	10	44	-12	42	44	46	49	50	51
Investment and Treasury	46	44	11	27	34	16	19	106	6	16	-38	64	-5	25	-32	-70	-41	-34
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	0	0
Pre-tax profit	106	163	162	154	159	157	157	47	13	9	-106	85	85	88	93	141	129	148
Retail	24	59	88	72	86	97	84	42	37	54	3	62	88	44	94	178	136	151
Corporate	40	56	62	60	40	48	53	-99	-33	-64	-69	-44	2	20	30	31	35	29
Investment and Treasury	42	47	13	22	33	15	20	104	9	19	-39	67	-5	24	-31	-71	-41	-33
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	3	0	0

Source: Company reports, Citi Investment Research and Analysis

Annual Financials

Figure 111. Millennium – Profit and Loss, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	480.1	650.5	35.5%	771.7	18.6%	980.9	27.1%	598.5	-39.0%	927.5	55.0%	1,127.2	21.5%	1,098.0	-2.6%
Net Fee & Commission Income	264.8	365.2	37.9%	543.2	48.8%	472.0	-13.1%	493.8	4.6%	564.9	14.4%	595.0	5.3%	643.3	8.1%
Financial Income	208.2	53.3	-74.4%	91.2	71.2%	149.8	64.3%	274.5	83.2%	92.8	-66.2%	64.8	-30.2%	140.4	116.8%
Other Income	111.4	198.6	78.3%	303.3	52.7%	245.9	-18.9%	87.1	-64.6%	131.1	50.6%	115.2	-12.1%	136.9	18.8%
Total Revenue	1,064.5	1,267.6	19.1%	1,709.4	34.9%	1,848.6	8.1%	1,453.9	-21.4%	1,716.3	18.0%	1,902.2	10.8%	2,018.6	6.1%
Labour Costs	-326.3	-412.9	26.5%	-538.8	30.5%	-609.0	13.0%	-470.7	-22.7%	-525.9	11.7%	-547.8	4.2%	-573.7	4.7%
General Costs	-343.8	-382.9	11.4%	-431.1	12.6%	-510.2	18.3%	-472.0	-7.5%	-481.1	1.9%	-518.3	7.7%	-567.7	9.5%
Depreciation	-85.8	-61.5	-28.4%	-87.1	41.7%	-70.4	-19.2%	-79.6	13.1%	-74.6	-6.3%	-68.1	-8.7%	-69.0	1.2%
Operating Expenses	-755.9	-857.2	13.4%	-1,057.0	23.3%	-1,189.6	12.5%	-1,022.4	-14.1%	-1,081.6	5.8%	-1,134.2	4.9%	-1,210.4	6.7%
Operating Profit	308.7	410.4	32.9%	652.3	59.0%	659.0	1.0%	431.5	-34.5%	634.7	47.1%	767.9	21.0%	808.3	5.3%
Provision Charge	-15.4	-39.6	156.9%	-67.8	71.1%	-137.3	102.5%	-436.7	218.1%	-226.9	-48.0%	-183.6	-19.1%	-442.9	141.3%
Extraordinary Profit/(Loss)	416.5	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na
Associate Income	0.0	0.0	na	0.0	na	0.0	na	7.0	na	0.0	na	-0.6	na	-0.8	33.3%
Profit Before Tax	709.7	370.7	-47.8%	584.6	57.7%	521.7	-10.7%	1.9	-99.6%	407.8	21649%	583.7	43.1%	364.5	-37.6%
Minorities	0.0	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na
Tax	-142.7	-69.9	-51.0%	-123.0	75.8%	-108.3	-11.9%	-0.4	-99.6%	-81.8	21428%	-121.7	48.8%	-72.9	-40.1%
Net Profit	567.1	300.8	-47.0%	461.6	53.5%	413.4	-10.4%	1.5	-99.6%	326.0	21706%	462.0	41.7%	291.6	-36.9%
EPS (Zl)	0.6	0.3	-47.0%	0.5	53.5%	0.4	-10.4%	0.0	-99.6%	0.3	19230%	0.4	27.3%	0.2	-36.9%
DPS (Zl)	0.5	0.1	-68.5%	0.2	11.8%	0.0	-100.0%	0.0	0.0%	0.1	100%	0.2	52.3%	0.1	-21.1%
Average Diluted Number of Shares (m)	965.7	965.7	0.0%	965.7	0.0%	965.7	0.0%	965.7	0.0%	1,089.4	12.8%	1,213.1	11.4%	1,213.1	0.0%

Source: Company reports, CIRA estimates

Figure 112. Millennium – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2010E	chg	2012E	chg
Cash and NBP Balances	511	966	89.1%	1,257	30.2%	1,803	43.4%	2,191	21.6%	2,051	-6.4%	2,092	2.0%	2,134	2.0%
Interbank placements	2,914	1,139	-60.9%	1,082	-5.0%	1,641	51.7%	904	-44.9%	1,541	70.4%	1,572	2.0%	1,604	2.0%
Financial Assets & Securities	8,222	6,782	-17.5%	5,247	-22.6%	9,204	75.4%	7,573	-17.7%	6,018	-20.5%	5,423	-9.9%	5,718	5.4%
Net client lending	9,592	14,938	55.7%	22,027	47.5%	33,748	53.2%	33,485	-0.8%	36,738	9.7%	42,931	16.9%	46,014	7.2%
Fixed assets	232	297	28.0%	337	13.6%	385	14.1%	347	-10.0%	242	-30.2%	244	1.0%	247	1.0%
Other assets	680	570	-16.1%	579	1.5%	334	-42.3%	413	23.5%	394	-4.6%	548	39.1%	598	9.2%
Total Assets	22,151	24,692	11.5%	30,530	23.6%	47,115	54.3%	44,913	-4.7%	46,984	4.6%	52,810	12.4%	56,315	6.6%
Interbank borrowing	4,128	5,028	21.8%	3,295	-34.5%	4,563	38.5%	7,252	58.9%	2,755	-62.0%	3,719	35.0%	3,794	2.0%
Client deposits	13,994	16,069	14.8%	21,801	35.7%	31,702	45.4%	31,559	-0.5%	35,395	12.2%	38,722	9.4%	41,913	8.2%
Other liabilities	1,638	1,379	-15.8%	2,915	111.3%	8,035	175.7%	3,316	-58.7%	4,743	43.0%	5,989	26.3%	6,120	2.2%
Minorities	0	0	na	0	na	0	na	0	na	0	na	0	na	0	na
Equity (ex Minorities)	2,391	2,215	-7.3%	2,520	13.8%	2,815	11.7%	2,787	-1.0%	4,091	46.8%	4,380	7.1%	4,487	2.4%
Total liabilities & Equity	22,151	24,692	11.5%	30,530	23.6%	47,115	54.3%	44,914	-4.7%	46,984	4.6%	52,810	12.4%	56,315	6.6%
Interest Earning Assets	21,239	23,825	12.2%	29,614	24.3%	46,396	56.7%	44,154	-4.8%	46,349	5.0%	52,018	12.2%	55,470	6.6%
BVPS (Zl)	2.48	2.29	-7.3%	2.61	13.8%	2.91	11.7%	2.89	-1.0%	3.37	16.8%	3.61	7.1%	3.70	2.4%

Source: Company reports, CIRA estimates

Figure 113. Millennium – Key Ratios, 2005-2012E (Percentage)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	2.38%	2.89%	2.89%	2.58%	1.32%	2.05%	2.29%	2.04%
NIM on Total Ave. Assets	2.27%	2.78%	2.79%	2.53%	1.30%	2.02%	2.26%	2.01%
Net Fee & Commission Income/Total Income	24.9%	28.8%	31.8%	25.5%	34.0%	32.9%	31.3%	31.9%
Net Fee & Commission Income/Deposits	1.9%	2.3%	2.5%	1.5%	1.6%	1.6%	1.5%	1.5%
Cost/Income	71.0%	67.6%	61.8%	64.4%	70.3%	63.0%	59.6%	60.0%
Cost/Avg. Assets	3.6%	3.7%	3.8%	3.1%	2.2%	2.4%	2.3%	2.2%
Effective tax rate	20.1%	18.9%	21.0%	20.8%	20.3%	20.1%	20.8%	20.0%
Dividend Payout Ratio	80.9%	48.0%	35.0%	0.0%	0.0%	37.2%	40.0%	50.0%
Provisions/Avg Net Loans	0.18%	0.32%	0.37%	0.49%	1.30%	0.65%	0.46%	1.00%
Equity/Assets	10.8%	9.0%	8.3%	6.0%	6.2%	8.7%	8.3%	8.0%
Loans/Deposits	68.5%	93.0%	101.0%	106.5%	106.1%	103.8%	110.9%	109.8%
Loans/Total Assets	43.3%	60.5%	72.1%	71.6%	74.6%	78.2%	81.3%	81.7%
ROE	25.9%	13.1%	19.5%	15.5%	0.1%	9.5%	10.9%	6.6%
ROA	2.68%	1.28%	1.67%	1.06%	0.00%	0.71%	0.93%	0.53%
NPLs/Total Loans	10.0%	5.7%	3.4%	3.4%	5.9%	5.8%	5.8%	5.5%
Provision Coverage of NPLs	65.1%	74.8%	79.5%	64.4%	54.4%	54.1%	40.9%	52.3%
RWA/Total Assets	49.8%	64.4%	68.4%	73.5%	68.8%	67.6%	69.0%	75.0%
CAR	19.1%	13.6%	13.7%	10.2%	11.3%	14.4%	12.8%	11.3%
Group Employees	4,484	5,089	6,067	7,049	6,245	6,135	6,144	6,144

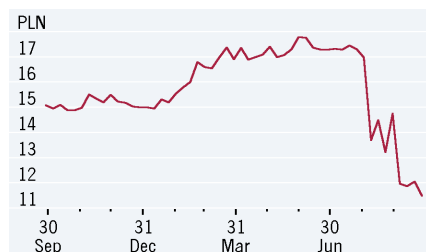
Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Sell/Medium Risk	3M
Price (29 Sep 11)	ZL12.75
Target price	ZL12.00
from ZL16.10	
Expected share price return	-5.9%
Expected dividend yield	0.0%
Expected total return	-5.9%
Market Cap	ZL3,464M
	US\$1,055M

Price Performance (RIC: BKRE.WA, BB: KRB PW)



Kredyt Bank SA (BKRE.WA)

Fundamental View Negative, M&A Upside Risk: Maintaining Sell

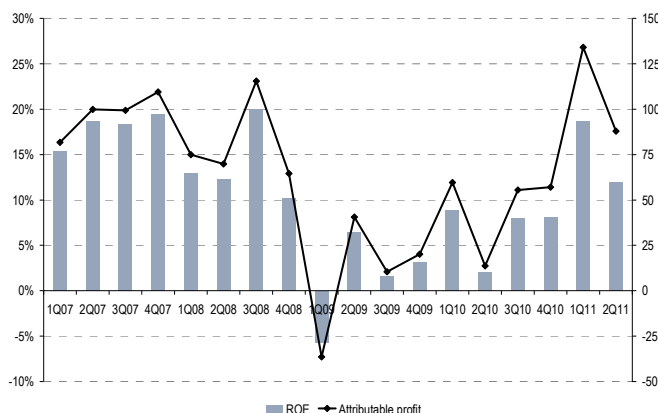
- **Sold in Bilateral Negotiations?** — According to the *Gazeta Wyborcza* daily, Santander has just completed due diligence in Kredyt Bank and has made an offer for the bank. KBC is expected to respond soon; if it doesn't accept the offer it will start a regular tender, according to the report. Previously the newspaper speculated that Santander pushed KBC to enter into bilateral negotiations instead of an open tender. The newspaper noted also that Merrill Lynch, close to Santander, is KBC's advisor in the sale process. None of the companies in question have commented.
- **Attractive M&A Target** — Were Kredyt Bank acquired inexpensively (which, in our view, given the low quality of the business, might be the case in the absence of an open tender) by Santander, it would create the third-biggest bank in Poland in every category while cost synergy potential would be material, in our view.
- **M&A Risk to Fundamental View** — According to Polish law exceeding a 66% threshold in a listed stock triggers an obligation to announce a public tender for 100% of shares. As KBC holds an 80% stake in Kredyt Bank, the buyer of its stake should announce a public tender and offer a price not lower than the highest of (1) the price paid to KBC, (2) the 3 month average and (3) the 6 month average. This implies a minimum ZL 15.96 tender price. Despite the material upside risk to our fundamental view, we stick to our fundamental valuation of the bank because (1) a buyer could try to avoid the tender announcement by buying a company to which KBC transfers less than 66% of shares of Kredyt Bank (as GE did when it bought BPH in 2007) (2) any transaction could be delayed or cancelled due to market conditions.
- **2012E EPS Cut by 70%** — We reduce our NIM estimates to 2.47% from 2.60% in 2012 and to 2.40% from 2.60% in 2013, lower our loan growth forecasts to 4% from 13% (in both years) and increase our cost of risk to 170bp from 120bp in 2012 and to 170bp from 100bp in 2013. These changes lead us to cut r EPS estimates by 70% and 78%, respectively.
- **Maintaining Sell** — We maintain our assumption of sustainable ROE of 12.5% but due to lowered 2012 and 2013 EPS estimates and an increased cost of risk assumption (to 11.5% from 10.5%, in line with assumptions for other banks with material exposure to CHF loans), we decrease our target price to ZL 12.0 from ZL 16.10. We maintain our Sell/Medium Risk (3M) rating.

Kredyt Bank SA (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	34.6	185.9	342.1	93.7	96.6
Diluted EPS (ZL)	0.13	0.68	1.26	0.34	0.36
Diluted EPS (Old) (ZL)	0.13	0.68	1.26	1.14	1.62
PE (x)	100.2	18.6	10.1	37.0	35.9
P/BV (x)	1.3	1.2	1.1	1.1	1.1
DPS (ZL)	0.00	0.37	0.00	0.00	0.18
Net Div Yield (%)	0.0	2.9	0.0	0.0	1.4
ROE (%)	1.3	6.9	11.6	3.0	3.0

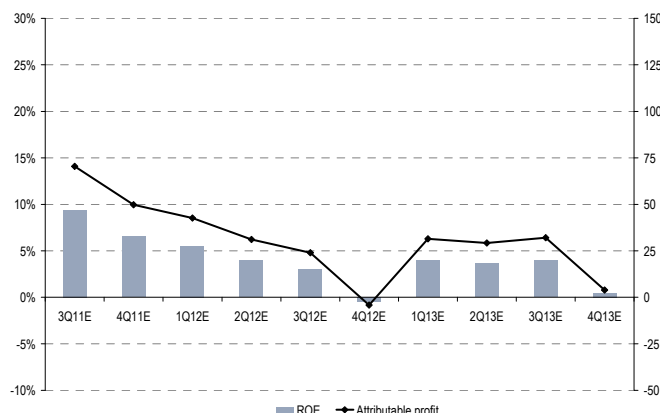
Kredyt Bank in Snapshots

Figure 114. Kredyt Bank – Reported Net Profit and ROE, 1Q07-2Q11 (Polish Zloty in million/Percentage)



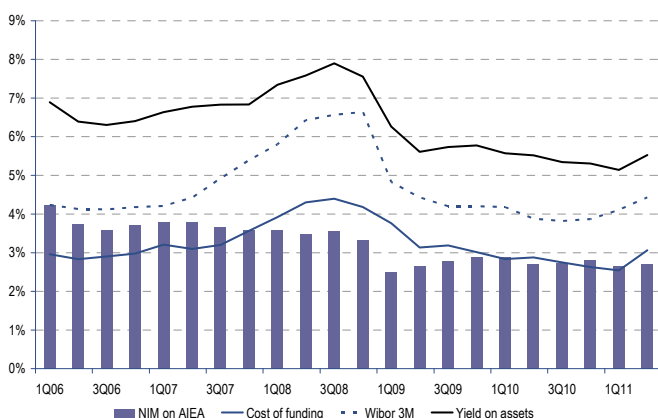
Source: Company reports, Citi Investment Research and Analysis

Figure 115. Kredyt Bank – Forecast Net Profit and ROE, 3Q11E-4Q13E (Polish Zloty in million/Percentage)



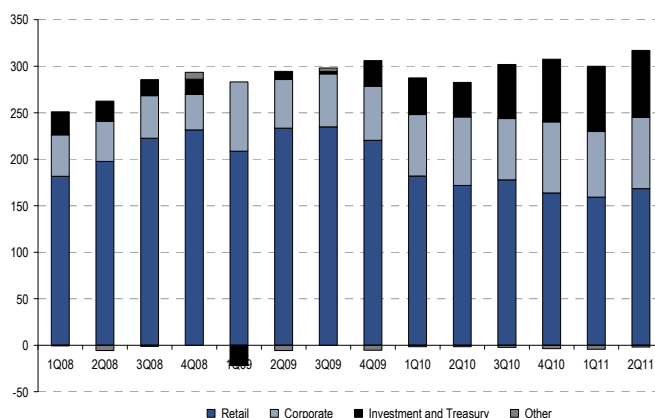
Source: Citi Investment Research and Analysis

Figure 116. Kredyt Bank – Yield on Assets and Cost of Funding, 1Q06-2Q11 (Percentage)



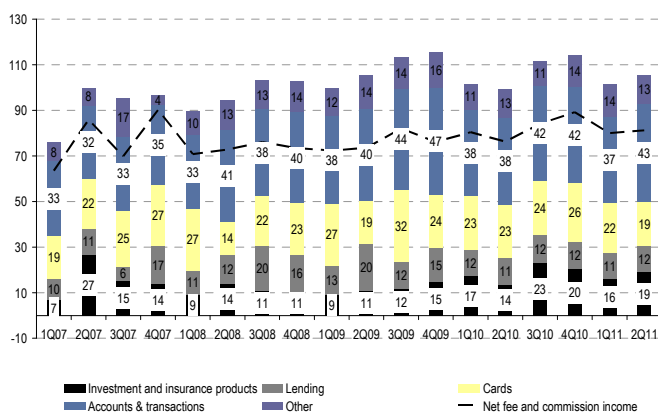
Source: Company reports, Citi Investment Research and Analysis

Figure 117. Kredyt Bank – Net Interest Income by Divisions, 1Q08-2Q11 (Polish Zloty in million)



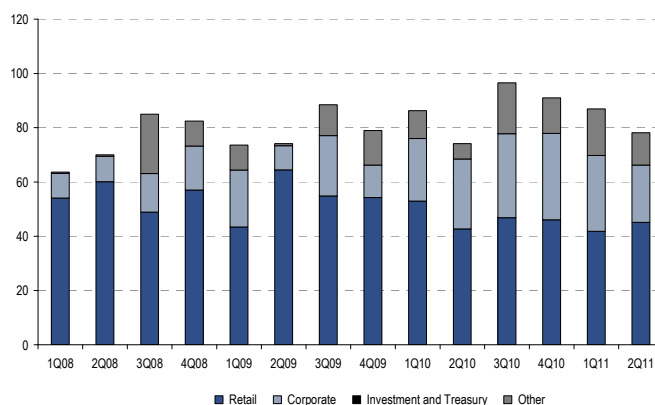
Source: Company reports, Citi Investment Research and Analysis

Figure 118. Kredyt Bank – Breakdown of Fee Income, 1Q07-2Q11 (Polish Zloty in million)



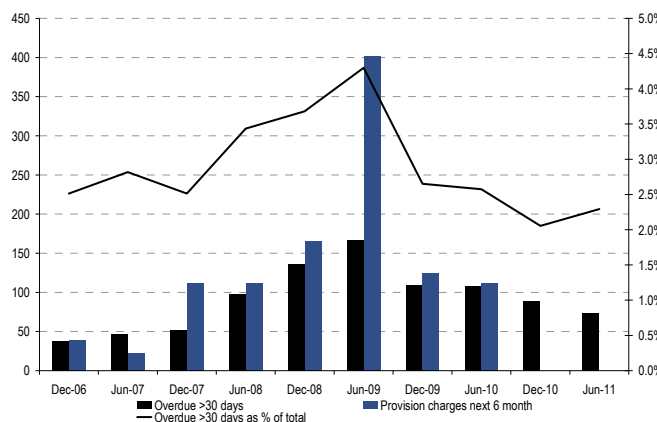
Source: Company reports, Citi Investment Research and Analysis

Figure 119. Kredyt Bank – Net Fees by Divisions, 1Q08-2Q11 (Polish Zloty in million)



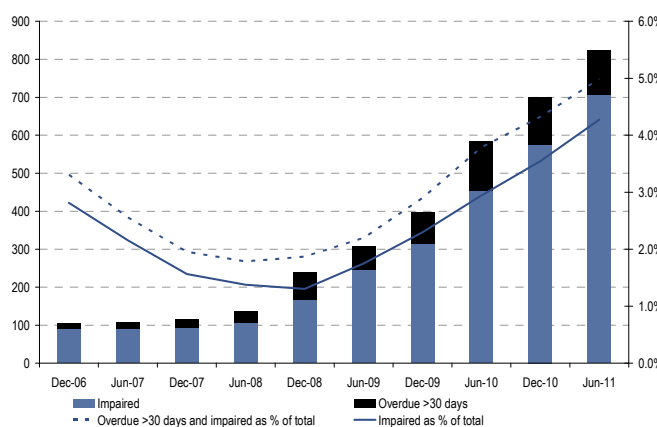
Source: Company reports, Citi Investment Research and Analysis

Figure 120. Kredyt Bank – Overdue Consumer Loans vs. Provisions, Dec 06-Jun 11 (Polish Zloty in million)



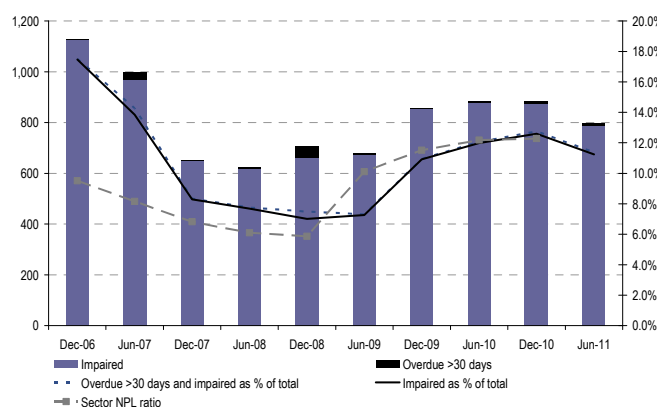
Source: Company reports, Citi Investment Research and Analysis

Figure 122. Kredyt Bank – Overdue and Impaired Mortgage Loans, Dec 06-Jun 11 (Polish Zloty in million)



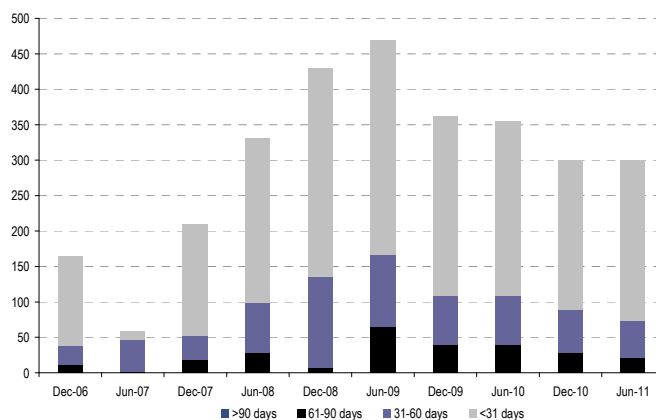
Source: Company reports, Citi Investment Research and Analysis

Figure 124. Kredyt Bank – Overdue and Impaired Corporate Loans, Dec 06-Jun 11 (Polish Zloty in million)



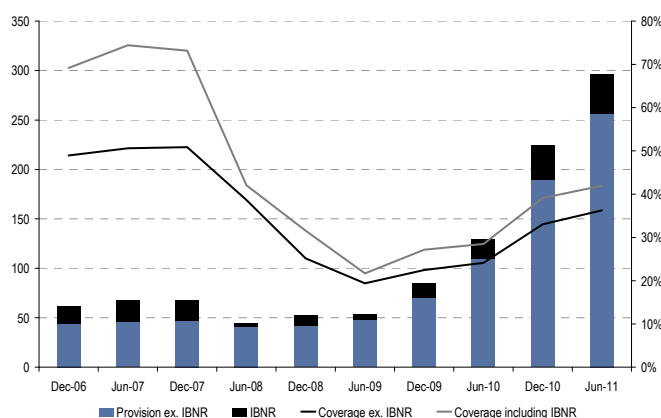
Source: Company reports, Citi Investment Research and Analysis

Figure 121. Kredyt Bank – Overdue Consumer Loans, Dec 06-Jun 11 (Polish Zloty in million)



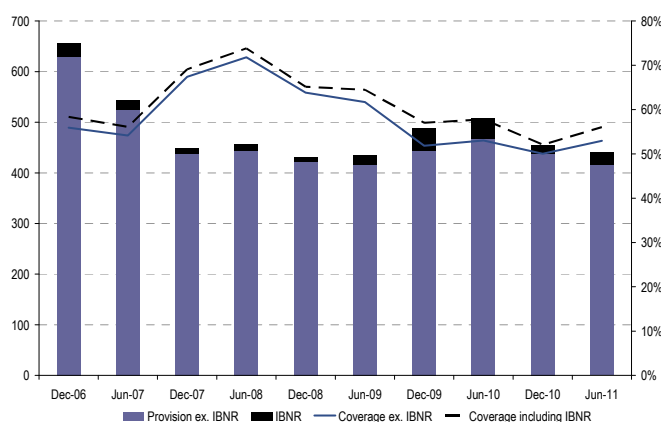
Source: Company reports, Citi Investment Research and Analysis

Figure 123. Kredyt Bank – Provision On Mortgage Loans, Dec 06-Jun 11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Figure 125. Kredyt Bank – Provision On Corporate Loans, Dec 06-Jun 11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 126. Kredyt Bank – Segment Breakdown, 1Q08–2Q11 (Polish Zloty in million)

	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11
Nil	250.2	256.9	284.5	293.4	261.1	288.9	298.1	300.7	285.9	281.3	299.6	303.9	295.6	315.3
Retail	181.5	197.7	222.6	231.6	208.7	233.5	234.7	220.3	182.0	171.8	177.7	163.6	159.2	168.3
Corporate	44.8	43.0	45.7	38.0	74.3	52.4	57.1	58.2	66.0	73.7	66.0	76.5	70.7	76.6
Investment and Treasury	24.7	21.8	17.3	16.5	-21.3	8.7	2.6	27.6	39.5	37.3	58.2	67.4	70.2	72.1
Other	-0.8	-5.6	-1.2	7.3	-0.7	-5.6	3.7	-5.4	-1.5	-1.4	-2.3	-3.7	-4.5	-1.8
Fees	63.7	70.0	85.0	82.5	73.6	74.1	88.4	78.9	86.3	74.1	96.6	91.0	86.9	78.2
Retail	54.1	60.1	48.9	57.0	43.4	64.5	54.8	54.3	53.0	42.7	46.8	46.0	41.8	45.1
Corporate	9.1	9.3	14.2	16.2	21.0	8.9	22.3	12.0	23.1	25.8	30.9	31.9	28.0	21.1
Investment and Treasury	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.5	0.6	21.9	9.2	9.2	0.7	11.3	12.7	10.2	5.6	18.8	13.1	17.1	11.9
Total Income	372.7	384.6	451.4	427.1	414.3	423.7	422.5	675.5	395.7	391.7	428.2	412.7	397.6	403.3
Retail	257.4	288.6	324.7	345.5	257.0	288.3	301.9	286.8	241.7	227.8	239.8	221.3	210.1	224.8
Corporate	70.7	72.9	75.4	65.8	109.0	96.7	88.2	77.9	101.4	111.5	107.6	121.2	109.6	109.9
Investment and Treasury	37.1	38.3	26.3	4.1	28.3	24.6	15.3	33.8	44.3	46.0	64.3	61.7	64.7	60.1
Other	7.5	-15.2	25.0	11.7	20.0	14.1	17.1	277.0	8.3	6.4	16.5	8.4	13.3	8.5
Total costs	-248.1	-287.7	-268.9	-299.8	-270.4	-247.9	-245.3	-259.9	-224.9	-227.0	-234.8	-241.4	-232.3	-240.2
Retail	-210.0	-251.3	-234.1	-264.2	-217.3	-209.8	-205.4	-219.4	-166.9	-170.4	-171.8	-178.2	-167.2	-172.1
Corporate	-22.8	-26.2	-22.2	-23.9	-34.6	-22.5	-24.7	-26.6	-39.8	-43.1	-45.3	-47.6	-47.8	-51.6
Investment and Treasury	-11.5	-6.7	-8.1	-8.4	-13.1	-9.5	-9.3	-8.4	-12.2	-7.9	-11.3	-9.4	-11.8	-10.7
Other	-3.8	-3.5	-4.5	-3.3	-5.6	-6.1	-5.9	-5.6	-6.0	-5.6	-6.4	-6.2	-5.4	-5.8
Cost/Income	67%	75%	60%	70%	65%	58%	58%	38%	57%	58%	55%	59%	58%	60%
Retail	82%	87%	72%	76%	85%	73%	68%	76%	69%	75%	72%	81%	80%	77%
Corporate	32%	36%	29%	36%	32%	23%	28%	34%	39%	39%	42%	39%	44%	47%
Investment and Treasury	31%	18%	31%	204%	46%	39%	60%	25%	28%	17%	18%	15%	18%	18%
Other	51%	-23%	18%	29%	28%	43%	35%	2%	72%	88%	39%	73%	41%	68%
Operating income	124.6	96.9	182.5	127.3	143.8	175.9	177.2	415.5	170.8	164.7	193.5	171.2	165.3	163.1
Retail	47.4	37.3	90.6	81.4	39.8	78.5	96.5	67.5	74.9	57.4	68.0	43.0	42.9	52.7
Corporate	47.9	46.6	53.2	41.9	74.4	74.2	63.5	51.3	61.5	68.3	62.3	73.6	61.7	58.3
Investment and Treasury	25.6	31.6	18.2	-4.3	15.3	15.1	6.1	25.4	32.0	38.1	53.0	52.4	52.8	49.4
Other	3.7	-18.6	20.5	8.3	14.4	8.0	11.1	271.4	2.4	0.8	10.1	2.2	7.9	2.7
Net Provisioning	-24.1	-9.0	-37.0	-38.1	-190.9	-127.5	-162.0	-387.2	-92.8	-145.3	-118.3	-112.3	11.2	-44.4
Retail	-39.5	-17.4	-51.2	-53.9	-76.2	-100.5	-142.1	-320.6	-80.8	-91.9	-139.9	-73.6	8.7	-40.6
Corporate	6.5	-24.5	26.7	-37.3	-113.4	-31.3	-15.7	-62.9	-2.7	-48.1	23.3	-31.4	4.5	-11.6
Investment and Treasury	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	8.9	33.0	-12.5	53.0	-1.3	4.3	-4.2	-3.7	-9.3	-5.3	-1.7	-7.3	-1.9	7.9
Pre-tax profit	100.5	88.0	145.4	89.2	-47.1	48.4	15.2	28.3	78.0	19.4	75.2	59.0	176.5	118.7
Retail	7.9	19.9	39.4	27.5	-36.5	-21.9	-45.6	-253.2	-6.0	-34.5	-71.9	-30.6	51.6	12.1
Corporate	54.4	22.1	79.9	4.6	-38.9	42.9	47.8	-11.6	58.9	20.3	85.6	42.3	66.2	46.6
Investment and Treasury	25.6	31.6	18.2	-4.3	15.3	15.1	6.1	25.4	32.0	38.1	53.0	52.4	52.8	49.4
Other	12.6	14.4	8.0	61.3	13.0	12.3	7.0	267.6	-7.0	-4.5	8.5	-5.1	6.0	10.6

Source: Company reports, Citi Investment Research and Analysis

Annual Financials

Figure 127. Kredyt Bank – Profit and Loss, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	753.4	780.0	3.5%	871.5	11.7%	1,059.9	21.6%	1,061.2	0.1%	1,127.8	6.3%	1,198.4	6.3%	1,174.2	-2.0%
Net Fee & Commission Income	314.9	270.1	-14.2%	309.5	14.6%	293.1	-5.3%	304.1	3.7%	329.9	8.5%	345.3	4.7%	405.1	17.3%
Financial Income	91.8	40.4	-56.0%	47.9	18.5%	-276.2	na	-176.5	-36.1%	-608.9	245.0%	10.0	na	30.2	202.8%
Other Income	59.9	279.5	366.3%	216.1	-22.7%	559.1	158.7%	414.3	-25.9%	782.8	89.0%	146.6	-81.3%	137.8	-6.0%
Total Revenue	1,220.1	1,370.0	12.3%	1,445.0	5.5%	1,635.9	13.2%	1,603.1	-2.0%	1,631.6	1.8%	1,700.3	4.2%	1,747.3	2.8%
Labour Costs	-410.5	-438.5	6.8%	-492.5	12.3%	-536.2	8.9%	-454.1	-15.3%	-416.7	-8.2%	-437.4	5.0%	-464.9	6.3%
General Costs	-344.8	-379.4	10.0%	-371.4	-2.1%	-464.7	25.1%	-454.7	-2.1%	-410.5	-9.7%	-512.6	24.9%	-553.0	7.9%
Depreciation	-135.5	-112.4	-17.0%	-110.7	-1.5%	-103.7	-6.3%	-114.5	10.4%	-101.0	-11.8%	-96.5	-4.4%	-100.1	3.7%
Operating Expenses	-890.8	-930.2	4.4%	-974.6	4.8%	-1,105	13.3%	-1,023	-7.4%	-928.1	-9.3%	-1,046	12.8%	-1,118	6.8%
Operating Profit	329.3	439.8	33.6%	470.4	7.0%	531.3	13.0%	579.8	9.1%	703.5	21.3%	653.9	-7.1%	629.2	-3.8%
Provision Charge	-9.2	19.1	na	30.1	57.6%	-108.2	na	-803.2	642.3%	-472.0	-41.2%	-286.4	-39.3%	-513.5	79.3%
Extraordinary Profit/(Loss)	0.0	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na
Associate Income	1.2	1.7	38.8%	1.5	-12.6%	-2.0	na	1.8	na	3.2	76.8%	1.8	-44.0%	0.0	na
Profit Before Tax	321.4	460.6	43.3%	502.0	9.0%	421.1	-16.1%	-221.6	na	234.7	na	369.3	57.3%	115.7	-68.7%
Minorities	1.0	0.0	na	0.0	na	0.0	na	228.6	na	0.0	na	51.5	na	0.0	na
Tax	93.5	7.5	-92.0%	-111.4	na	-96.1	-13.7%	27.6	na	-48.8	na	-78.7	61.4%	-22.0	-72.1%
Net Profit	415.9	468.1	12.6%	390.5	-16.6%	324.9	-16.8%	34.6	-89.4%	185.9	438.0%	342.1	84.0%	93.7	-72.6%
EPS (Zl)	1.5	1.7	12.6%	1.4	-16.6%	1.2	-16.8%	0.1	-89.4%	0.7	438.0%	1.3	84.0%	0.3	-72.6%
DPS (Zl)	0.2	0.4	68.2%	0.5	40.5%	0.0	na	0.0	na	0.4	na	0.0	na	0.0	na
Average Diluted Number of Shares (m)	271.7	271.7	0.0%	271.7	0.0%	271.7	0.0%	271.7	0.0%	271.7	0.0%	271.7	0.0%	271.7	0.0%

Source: Company reports, CIRA estimates

Figure 128. Kredyt Bank – Balance Sheet, 2005-2012E (Polish Zloty in million)

GROUP	2005	2006	chg	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Cash and NBP Balances	607	641	5.5%	612	-4.5%	828	35.4%	1,175	42.0%	1,944	65.4%	1,983	2.0%	2,023	2.0%
Interbank placements	2,227	2,181	-2.1%	2,454	12.5%	339	-86.2%	520	53.5%	1,551	198.5%	1,582	2.0%	1,614	2.0%
Financial Assets & Securities	7,414	6,829	-7.9%	6,442	-5.7%	9,859	53.0%	10,696	8.5%	11,650	8.9%	13,346	14.6%	13,961	4.6%
Net client lending	9,702	11,550	19.0%	16,622	43.9%	26,733	60.8%	25,722	-3.8%	27,195	5.7%	29,611	8.9%	30,813	4.1%
Fixed assets	416	386	-7.4%	396	2.8%	422	6.4%	354	-16.2%	290	-17.8%	305	5.0%	311	2.0%
Other assets	475	646	35.9%	602	-6.9%	550	-8.5%	610	10.8%	744	22.1%	785	5.4%	823	4.9%
Total Assets	20,841	22,232	6.7%	27,128	22.0%	38,731	42.8%	39,077	0.9%	43,374	11.0%	47,611	9.8%	49,544	4.1%
Interbank borrowing	2,562	2,163	-15.6%	6,403	196.1%	13,247	106.9%	12,403	-6.4%	12,379	-0.2%	14,632	18.2%	14,267	-2.5%
Client deposits	14,534	15,551	7.0%	17,089	9.9%	20,275	18.6%	22,469	10.8%	25,661	14.2%	27,211	6.0%	28,316	4.1%
Other liabilities	2,064	2,426	17.6%	1,360	-43.9%	2,563	88.4%	1,615	-37.0%	2,506	55.1%	2,692	7.4%	3,792	40.9%
Minorities	0	0	na	0	na	0	na	0	na	0	na	0	na	0	na
Equity (ex Minorities)	1,682	2,092	24.4%	2,276	8.8%	2,646	16.2%	2,589	-2.2%	2,828	9.3%	3,076	8.8%	3,170	3.0%
Total liabilities & Equity	20,841	22,232	6.7%	27,128	22.0%	38,731	42.8%	39,077	0.9%	43,374	11.0%	47,611	9.8%	49,544	4.1%
Interest Earning Assets	19,949	21,200	na	26,130	na	37,758	na	38,113	na	42,340	na	46,522	na	48,411	na
BVPS (Zl)	6.19	7.70	na	8.38	na	9.74	na	9.53	na	10.41	na	11.32	na	11.67	na

Source: Company reports, CIRA estimates

Figure 129. Kredyt Bank – Key ratios, 2005-012E (Percentage)

GROUP	2005	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	3.77%	3.79%	3.68%	3.32%	2.80%	2.80%	2.70%	2.47%
NIM on Total Ave. Assets	3.61%	3.62%	3.53%	3.22%	2.73%	2.74%	2.63%	2.42%
Net Fee & Commission Income/Total Income	25.8%	19.7%	21.4%	17.9%	19.0%	20.2%	20.3%	23.2%
Net Fee & Commission Income/Deposits	2.2%	1.7%	1.8%	1.4%	1.4%	1.3%	1.3%	1.4%
Cost/Income	73.0%	67.9%	67.4%	67.5%	63.8%	56.9%	61.5%	64.0%
Cost/Avg. Assets	4.3%	4.3%	3.9%	3.4%	2.6%	2.3%	2.3%	2.3%
Effective tax rate	-29.1%	-1.6%	22.2%	22.8%	12.4%	20.8%	21.3%	19.0%
Dividend Payout Ratio	14.4%	21.5%	36.2%	0.0%	0.0%	54.1%	0.0%	0.0%
Provisions/Avg Net Loans	0.09%	-0.18%	-0.21%	0.50%	3.06%	1.78%	1.01%	1.70%
Equity/Assets	8.1%	9.4%	8.4%	6.8%	6.6%	6.5%	6.5%	6.4%
Loans/Deposits	66.8%	74.3%	97.3%	131.9%	114.5%	106.0%	108.8%	108.8%
Loans/Total Assets	46.6%	52.0%	61.3%	69.0%	65.8%	62.7%	62.2%	62.2%
ROE	26.0%	24.8%	17.9%	13.2%	1.3%	6.9%	11.6%	3.0%
ROA	1.99%	2.17%	1.58%	0.99%	0.09%	0.45%	0.75%	0.19%
NPLs/Total Loans	28.9%	13.5%	6.6%	4.9%	8.7%	9.7%	9.5%	7.5%
Provision Coverage of NPLs	73.3%	63.5%	73.0%	68.7%	60.4%	67.8%	68.2%	91.5%
RWA/Total Assets	57.9%	65.1%	78.3%	78.5%	71.6%	65.7%	70.0%	70.0%
CAR	16.4%	13.7%	9.7%	8.8%	11.8%	12.5%	11.4%	13.9%
Group Employees	6,477	6,583	6,724	7,050	4,896	4,834	4,897	4,897

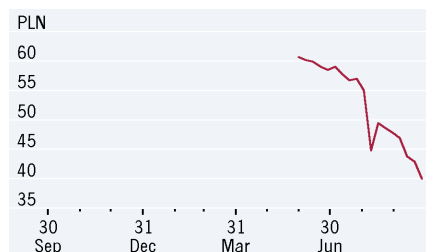
Source: Company reports, CIRA estimates

Company Focus

- Company Update
- Target Price Change
- Estimate Change

Buy/Low Risk	1L
Price (29 Sep 11)	ZL39.89
Target price	ZL60.30
	from ZL66.80
Expected share price return	51.2%
Expected dividend yield	0.0%
Expected total return	51.2%
Market Cap	ZL1,721M
	US\$524M

Price Performance (RIC: BGZ.WA, BB: BGZ PW)



BGZ (BGZ.WA)

Clients Resilient But Bank Leveraged to Growth: Maintaining Buy

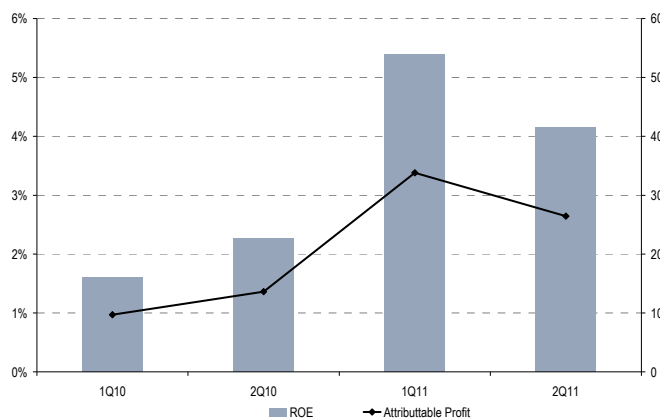
- **Food and Agri Are Defensive Industries** — The main clients of the bank, food producers and farmers, are relatively low-risk segments in turbulent times (as proved by low, 60bp, cost of risk in 2009). We also note that the recent depreciation of the Zloty is positive for Polish farmers receiving subsidies from EU as this leads to a higher, in Zloty terms, value of revenues.
- **Bank Leveraged to Growth** — The bank is in the middle of the process of opening new branches, which negatively affects the cost-to-income ratio (79% in 2Q11). The high cost base means that estimates of BGZ's earnings are highly sensitive to changes in revenue forecasts. The bank's still weak retail franchise leads to a low level of retail current accounts in total deposits (just 7%) and makes the bank dependent on funding through retail and corporate term deposits.
- **Rabobank Support Matters** — Long-term funding (CHF 1bn 12 year loan) received from Rabobank in 2Q11 not only strengthens the bank's funding position but also led to a change in the P&L structure as previously Swiss Franc mortgages were funded by Zloty deposits and FX Swaps or CIRS and the result of hedging instruments was booked in trading income, not in net interest income.
- **2012E EPS Cut by 68%** — We reduce our NIM estimates to 2.56% from 2.64% in 2012 and to 2.59% from 2.64 in 2013, lower our loan growth forecast to 12% from 15% (in both years) and increase cost of risk to 90bp from 70bp (in both years). These changes lead us to cut EPS estimates by 68% and 53%, respectively.
- **Maintaining Buy** — We maintain our assumption of sustainable ROE of 11% but due to lowered 2012 and 2013 EPS estimates we decrease our target price to ZL 60.3 from ZL 66.8. We maintain our Buy/Low Risk (1L) rating.

BGZ (PLN)

Year to 31 Dec	2009A	2010A	2011E	2012E	2013E
Net Income (ZLM)	100.6	112.3	69.3	59.1	123.6
Diluted EPS (ZL)	2.33	2.60	1.61	1.37	2.87
Diluted EPS (Old) (ZL)	2.33	2.60	2.42	4.24	6.08
PE (x)	17.1	15.3	24.8	29.1	13.9
P/BV (x)	0.7	0.7	0.7	0.7	0.6
DPS (ZL)	0.00	0.00	0.00	0.00	0.00
Net Div Yield (%)	0.0	0.0	0.0	0.0	0.0
ROE (%)	4.3	4.6	2.7	2.3	4.6

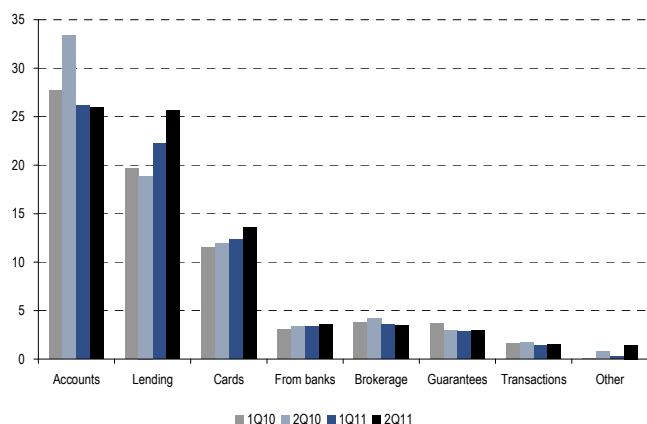
BGZ in Snapshots

Figure 130. BGZ – Reported Net Profit and ROE, 1Q10-2Q11 (Polish Zloty in million/Percentage)



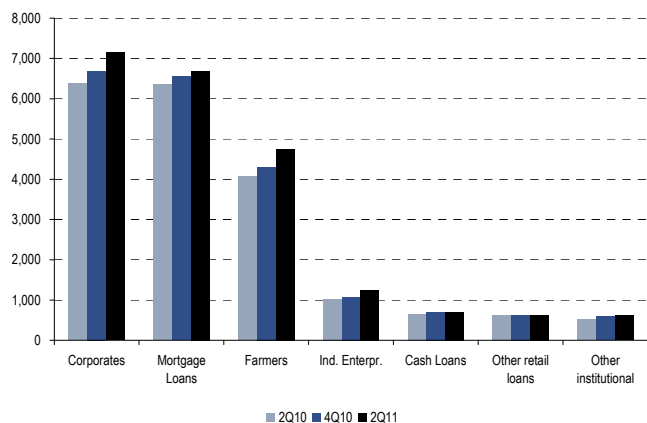
Source: Company reports, Citi Investment Research and Analysis

Figure 132. BGZ – Breakdown of Fee Income, 1Q10-2Q11 (Polish Zloty in million)



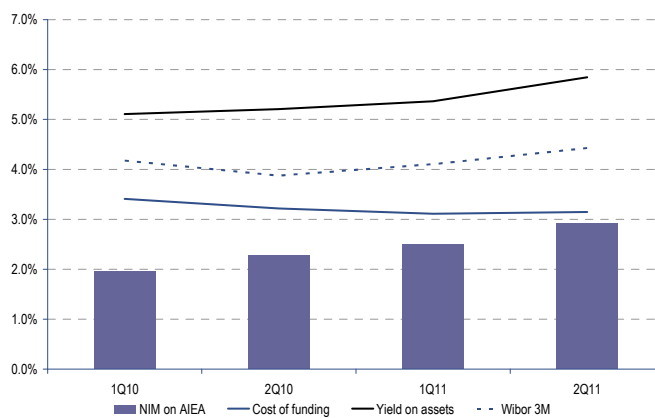
Source: Company reports, Citi Investment Research and Analysis

Figure 134. BGZ – Breakdown of Loans, 2Q10-2Q11 (Polish Zloty in million)



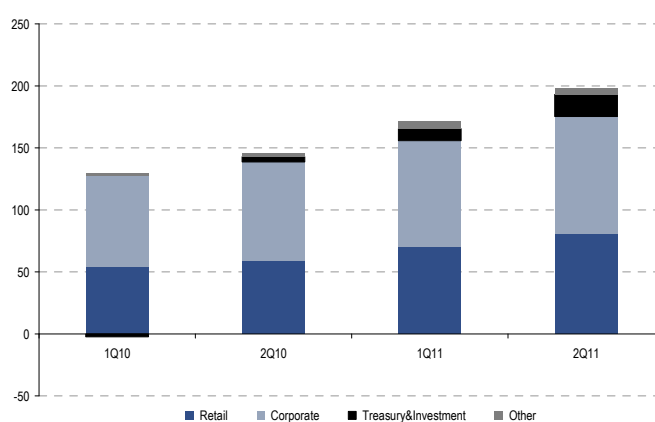
Source: Company reports, Citi Investment Research and Analysis

Figure 131. BGZ – Yield on Assets and Cost of Funding, 1Q10-2Q11 (Percentage)



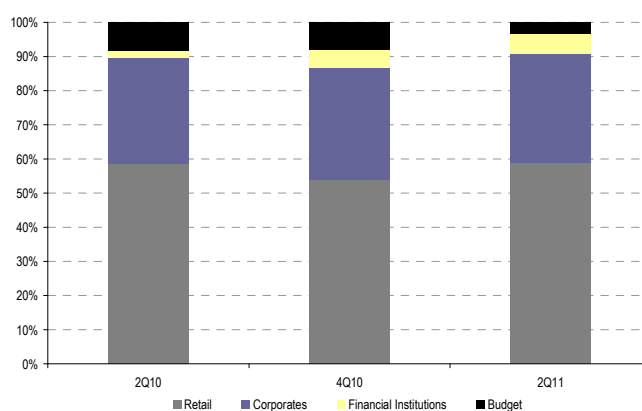
Source: Company reports, Citi Investment Research and Analysis

Figure 133. BGZ – Net Interest Income by Divisions, 1Q10-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 135. BGZ – Deposits Structure, 2Q10-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Segment Breakdown

Figure 136. BGZ – Segment Breakdown, 1Q10–2Q11 (Polish Zloty in million)

	1Q10	2Q10	1Q11	2Q11
Nil	127.199	146.015	171.14	198.639
Retail	53.981	59.496	70.524	80.903
Corporate	73.261	79.279	85.356	94.448
Treasury&Investment	-2.375	4.134	9.603	17.853
Other	2.332	3.106	5.657	5.435
Fees	62.919	68.82	64.061	68.191
Retail	22.455	23.613	21.235	19.944
Corporate	39.808	44.014	43.050	47.806
Treasury&Investment	-1.050	-0.228	-1.350	-0.764
Other	1.706	1.421	1.126	1.205
Total Income	219.362	246.873	275.813	300.157
Retail	79.889	86.970	96.087	105.108
Corporate	121.028	132.001	137.434	152.533
Treasury&Investment	15.583	17.271	33.885	19.840
Other	2.862	10.631	8.407	22.676
Total Costs	-185.161	-187.002	-217.819	-230.436
Retail	-98.282	-99.445	-111.807	-118.607
Corporate	-76.561	-77.547	-88.932	-97.849
Treasury&Investment	-6.144	-5.817	-9.613	-0.536
Other	-4.174	-4.193	-7.467	-13.444
Cost/Income	84%	76%	79%	77%
Retail	123%	114%	116%	113%
Corporate	63%	59%	65%	64%
Treasury&Investment	39%	34%	28%	3%
Other	146%	39%	89%	59%
Operating Income	34.201	59.871	57.994	69.721
Retail	-18.393	-12.475	-15.720	-13.499
Corporate	44.467	54.454	48.502	54.684
Treasury&Investment	9.439	11.454	24.272	19.304
Other	-1.312	6.438	0.940	9.232
Net Provisioning	-26.161	-48.625	-18.362	-35.286
Retail	-16.668	-34.360	-11.059	-18.886
Corporate	-7.209	-10.971	-1.606	-8.433
Treasury&Investment	0.906	0.641	4.720	-4.780
Other	-3.190	-3.935	-10.417	-3.187
Pre-tax Profit	8.04	11.246	39.632	34.435
Retail	-35.061	-46.835	-26.779	-32.385
Corporate	37.258	43.483	46.896	46.251
Treasury&Investment	10.345	12.095	28.992	14.524
Other	-4.502	2.503	-9.477	6.045

Source: Company data, Citi Investment Research and Analysis

Annual Financials

Figure 137. BGZ – Profit and Loss, 2006-2012E (Polish Zloty in million)

GROUP	2006	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Net Interest Income	489	572	16.9%	665	16.3%	462	-30.5%	604	30.8%	784	29.7%	803	2.4%
Net Fee & Commission Income	168	238	41.5%	217	-9.0%	248	14.6%	272	9.3%	276	1.7%	337	22.0%
Financial Income	37	95	160.9%	129	35.8%	203	57.3%	144	-29.4%	109	-24.1%	170	56.0%
Other Income	119	92	-23.1%	85	-7.3%	56	-34.3%	27	-51.4%	28	2.9%	36	28.8%
Total Revenue	813	997	22.6%	1,096	9.9%	970	-11.5%	1,047	7.9%	1,197	14.4%	1,346	12.4%
Labour Costs	-362	-388	7.3%	-414	6.5%	-369	-10.8%	-382	3.5%	-452	18.4%	-485	7.2%
General Costs	-248	-235	-5.2%	-294	25.2%	-305	3.6%	-332	8.9%	-439	32.4%	-481	9.5%
Depreciation	-95	-84	-11.4%	-68	-18.8%	-73	6.9%	-73	0.6%	-83	12.9%	-91	10.0%
Operating Expenses	-705	-707	0.4%	-776	9.7%	-747	-3.8%	-787	5.4%	-974	23.8%	-1,057	8.5%
Operating Profit	108	290	167.1%	320	10.5%	223	-30.3%	259	16.3%	223	-14.1%	289	29.7%
Provision Charge	-16	20	na	-45	na	-107	136.1%	-134	26.0%	-142	5.7%	-216	52.4%
Associate Income	0	0	na	0	na	0	-87.4%	2	na	4	149.5%	0	na
Profit Before Tax	92	310	236.8%	275	-11.3%	117	-57.6%	127	8.8%	85	-32.8%	73	-14.4%
Minorities	0	0	na	0	na	0	na	0	na	0	na	0	na
Tax	-7	-38	409.9%	-62	63.5%	-16	-74.2%	-15	-8.8%	-16	9.5%	-14	-12.8%
Net Profit	85	272	221.6%	213	-21.7%	101	-52.8%	112	11.6%	69	-38.3%	59	-14.7%
Dividends	0	0	na	0	na	0	na	0	na	0	na	0	na
Average Diluted Number of Shares (m)	37.0	40.1	8.3%	43.1	7.7%	43.1	0.0%	43.1	0.0%	43.1	0.0%	43.1	0.0%
EPS (Zl)	2.3	6.8	197.0%	4.9	-27.3%	2.3	-52.8%	2.6	11.6%	1.6	-38.3%	1.4	-14.7%
DPS (Zl)	0.0	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na	0.0	na

Source: Company reports, CIRA estimates

Figure 138. BGZ – Balance Sheet, 2006-2012E (Polish Zloty in million)

GROUP	2006	2007	chg	2008	chg	2009	chg	2010	chg	2011E	chg	2012E	chg
Cash and NBP Balances	315	498	58.1%	1,291	159.1%	1,279	-0.9%	1,380	7.8%	1,476	7.0%	1,580	7.0%
Interbank placements	3,929	1,717	-56.3%	799	-53.5%	357	-55.4%	281	-21.2%	253	-10.0%	228	-10.0%
Financial Assets & Securities	628	466	-25.8%	1,535	229.6%	797	-48.1%	2,688	237.3%	2,419	-10.0%	2,177	-10.0%
Net client lending	9,591	13,988	45.8%	17,066	22.0%	18,301	7.2%	19,869	8.6%	22,651	14.0%	25,369	12.0%
Fixed assets	441	427	-3.0%	449	5.2%	444	-1.1%	465	4.6%	511	10.0%	562	10.0%
Other assets	3,498	2,938	-16.0%	2,927	-0.4%	3,367	15.1%	3,947	17.2%	3,368	-14.7%	4,264	26.6%
Total Assets	18,402	20,034	8.9%	24,067	20.1%	24,546	2.0%	28,630	16.6%	30,678	7.2%	34,180	11.4%
Interbank borrowing	1,692	1,730	2.2%	1,149	-33.6%	476	-58.6%	1,020	114.4%	1,837	80.0%	1,469	-20.0%
Client deposits	14,073	15,542	10.4%	18,141	16.7%	19,599	8.0%	21,052	7.4%	20,841	-1.0%	23,967	15.0%
Other liabilities	1,130	692	-38.8%	2,499	261.3%	2,085	-16.6%	4,062	94.9%	5,436	33.8%	6,120	12.6%
Minorities	0	0	na	0	na	0	na	0	na	0	na	0	na
Equity (ex Minorities)	1,508	2,070	37.3%	2,278	10.1%	2,386	4.7%	2,495	4.6%	2,564	2.8%	2,623	2.3%
Total liabilities & Equity	18,402	20,034	8.9%	24,067	20.1%	24,546	2.0%	28,630	16.6%	30,678	7.2%	34,180	11.4%
Interest Earning Assets	17,699	19,359	9.4%	23,264	20.2%	23,728	2.0%	27,617	16.4%	29,624	7.3%	33,040	11.5%
BVPS (Zl)	41	48	17.8%	53	10.1%	55	4.7%	58	4.6%	59	2.8%	61	2.3%

Source: Company reports, CIRA estimates

Figure 139. BGZ – Key Ratios, 2006-2012E (Percentage)

GROUP	2006	2007	2008	2009	2010	2011E	2012E
NIM on AIEA	2.90%	3.09%	3.12%	1.97%	2.35%	2.74%	2.56%
NIM on Total Ave. Assets	2.79%	2.97%	3.02%	1.90%	2.27%	2.64%	2.48%
Net Fee & Commission Income/Total Income	20.7%	23.9%	19.8%	25.6%	25.9%	23.1%	25.0%
Net Fee & Commission Income/Deposits	1.2%	1.5%	1.2%	1.3%	1.3%	1.3%	1.4%
Cost/Income	86.7%	70.9%	70.8%	77.0%	75.2%	81.4%	78.5%
Cost/Avg. Assets	4.0%	3.7%	3.5%	3.1%	3.0%	3.3%	3.3%
Effective tax rate	8.0%	12.2%	22.5%	13.7%	11.4%	18.7%	19.0%
Dividend Payout Ratio	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Provisions/Avg Net Loans	0.2%	-0.2%	0.3%	0.6%	0.7%	0.7%	0.9%
Equity/Assets	8.2%	10.3%	9.5%	9.7%	8.7%	8.4%	7.7%
Loans/Deposits	68.2%	90.0%	94.1%	93.4%	94.4%	108.7%	105.8%
Loans/Total Assets	52.1%	69.8%	70.9%	74.6%	69.4%	73.8%	74.2%
ROE	5.9%	15.2%	9.8%	4.3%	4.6%	2.7%	2.3%
ROA	0.48%	1.42%	0.97%	0.41%	0.42%	0.23%	0.18%
NPLs/Total Loans	8.0%	3.9%	5.2%	5.8%	6.4%	6.0%	5.0%
Provision Coverage of NPLs	NA	88.6%	56.6%	55.0%	52.9%	57.2%	68.0%
RWA/Total Assets	59.0%	77.2%	79.9%	76.8%	71.5%	71.5%	71.5%
Tier I Ratio (%)	14.7%	11.3%	10.6%	11.5%	11.0%	10.8%	10.0%
CAR	14.7%	11.3%	10.9%	11.6%	11.1%	10.8%	12.0%

Source: Company reports, Citi Investment Research and Analysis

Appendix - Changes in Earning Estimates

Figure 140. Polish Banks – Changes to Net Loan Forecasts, 2011E-2013E (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	143,943	143,943	0.0%	158,879	155,809	-1.9%	175,364	168,653	-3.8%
Pekao	85,857	85,857	0.0%	96,643	92,941	-3.8%	108,782	100,609	-7.5%
BZ WBK	37,165	37,165	0.0%	42,646	40,229	-5.7%	47,998	43,545	-9.3%
Millennium	40,943	42,931	4.9%	46,082	46,014	-0.1%	51,866	49,319	-4.9%
Kredyt Bank	29,654	29,611	-0.1%	33,376	30,813	-7.7%	37,565	32,064	-14.6%
ING Bank Slaski	40,118	40,118	0.0%	45,153	44,283	-1.9%	49,838	48,880	-1.9%
BRE	65,015	65,015	0.0%	75,327	67,655	-10.2%	85,597	73,232	-14.4%
BGZ	21,454	21,899	2.1%	24,758	24,534	-0.9%	28,524	27,457	-3.7%
Total	464,151	466,540	0.5%	522,865	502,278	-3.9%	585,535	543,758	-7.1%

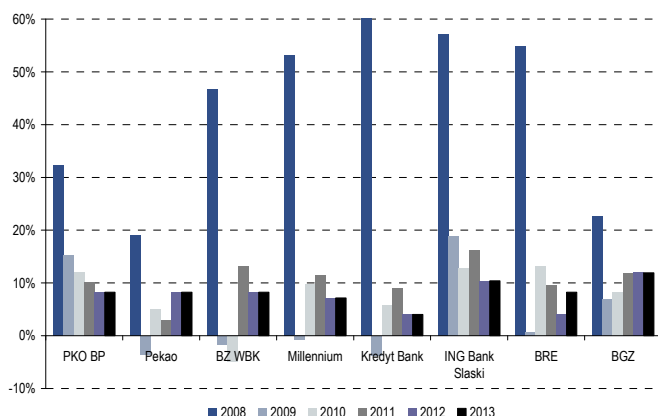
Source: Citi Investment Research and Analysis

Figure 141. Polish Banks – Changes to Deposit Forecasts, 2011E-2013E (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	145,422	145,422	0.0%	157,410	157,410	0.0%	170,385	168,715	-1.0%
Pekao	99,270	101,235	2.0%	107,453	109,580	2.0%	116,310	117,450	1.0%
BZ WBK	42,001	42,417	1.0%	45,463	45,913	1.0%	49,211	49,698	1.0%
Millennium	38,722	38,722	0.0%	43,581	41,913	-3.8%	49,051	45,369	-7.5%
Kredyt Bank	28,607	27,211	-4.9%	30,966	28,316	-8.6%	33,518	29,465	-12.1%
ING Bank Slaski	50,237	50,729	1.0%	53,845	54,373	1.0%	57,146	57,706	1.0%
BRE	49,755	47,381	-4.8%	56,543	49,305	-12.8%	64,258	52,846	-17.8%
BGZ	23,157	20,841	-10.0%	26,630	23,967	-10.0%	30,625	27,562	-10.0%
Total	477,170	473,958	-0.7%	521,891	510,778	-2.1%	570,504	548,812	-3.8%

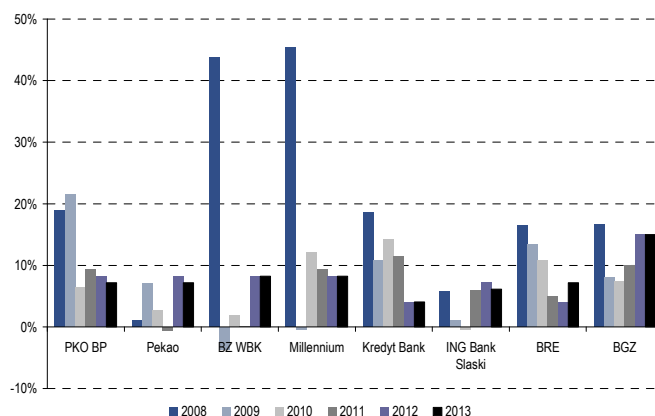
Source: Citi Investment Research and Analysis

Figure 142. Polish Banks – Loan Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 143. Polish Banks – Deposit Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 144. Polish Banks – Changes to Net Interest Income Forecasts, 2011E-2013E (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	7,384	7,367	-0.2%	7,918	7,784	-1.7%	8,609	8,305	-3.5%
Pekao	4,477	4,477	0.0%	4,947	4,407	-10.9%	5,411	4,694	-13.2%
BZ WBK	2,032	2,018	-0.7%	2,166	2,033	-6.1%	2,376	2,172	-8.6%
Millennium	1,147	1,127	-1.7%	1,292	1,098	-15.0%	1,376	1,171	-14.9%
Kredyt Bank	1,183	1,198	1.3%	1,237	1,174	-5.1%	1,356	1,185	-12.6%
ING Bank Slaski	1,825	1,826	0.0%	1,983	1,937	-2.3%	2,150	2,087	-2.9%
BRE	2,125	2,125	0.0%	2,308	2,019	-12.5%	2,549	2,115	-17.1%
BGZ	794	784	-1.3%	866	803	-7.3%	987	905	-8.2%
Total	20,968	20,922	-0.2%	22,716	21,255	-6.4%	24,813	22,633	-8.8%

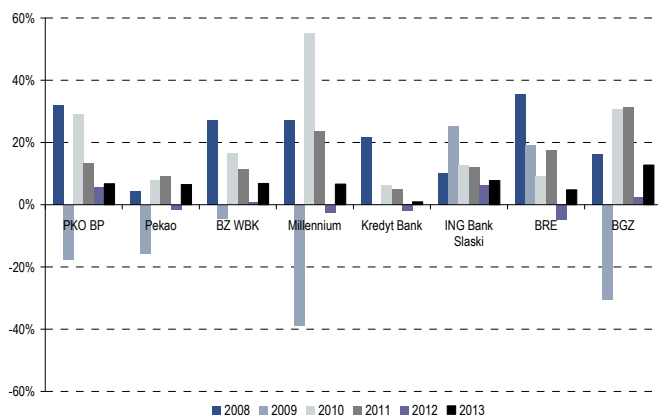
Source: Citi Investment Research and Analysis

Figure 145. Polish Banks – Changes to Net Fee Income Forecasts, 2011E-2013E (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	3,199	3,199	0.0%	3,478	3,478	0.0%	3,728	3,728	0.0%
Pekao	2,542	2,542	0.0%	2,747	2,747	0.0%	2,945	2,945	0.0%
BZ WBK	1,423	1,423	0.0%	1,558	1,558	0.0%	1,702	1,702	0.0%
Millennium	597	595	-0.3%	643	643	0.0%	701	701	0.0%
Kredyt Bank	352	345	-1.9%	405	405	0.0%	456	456	0.0%
ING Bank Slaski	1,034	1,037	0.3%	1,110	1,110	0.0%	1,201	1,201	0.0%
BRE	861	861	0.0%	968	968	0.0%	1,063	1,063	0.0%
BGZ	284	276	-2.7%	337	337	0.0%	404	404	0.0%
Total	10,292	10,278	-0.1%	11,246	11,246	0.0%	12,201	12,201	0.0%

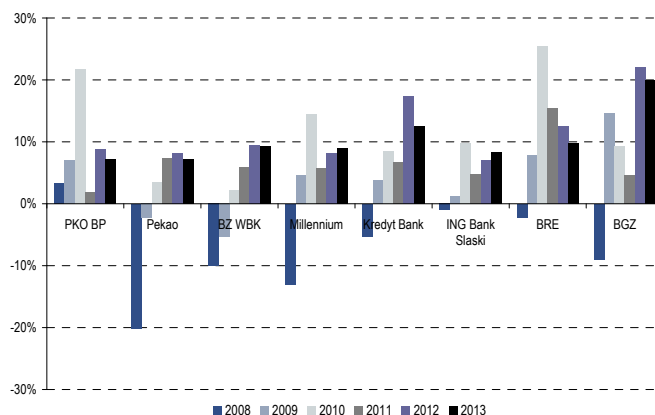
Source: Citi Investment Research and Analysis

Figure 146. Polish Banks – Net Interest Income Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 147. Polish Banks – Net Fees Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 148. Polish Banks – Changes to Total Revenue Forecasts, 2011E-2013E (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	11,056	11,039	-0.2%	11,970	11,836	-1.1%	12,922	12,618	-2.4%
Pekao	7,672	7,672	0.0%	8,442	7,902	-6.4%	9,145	8,428	-7.8%
BZ WBK	3,801	3,787	-0.4%	4,083	3,947	-3.3%	4,470	4,254	-4.8%
Millennium	1,916	1,902	-0.7%	2,169	2,019	-6.9%	2,346	2,184	-6.9%
Kredyt Bank	1,693	1,700	0.4%	1,810	1,747	-3.5%	2,000	1,829	-8.6%
ING Bank Slaski	2,976	2,944	-1.1%	3,221	3,181	-1.2%	3,479	3,427	-1.5%
BRE	3,518	3,518	0.0%	3,819	3,530	-7.6%	4,209	3,774	-10.3%
BGZ	1,273	1,201	-5.6%	1,409	1,346	-4.4%	1,607	1,526	-5.0%
Total	33,906	33,764	-0.4%	36,923	35,509	-3.8%	40,178	38,042	-5.3%

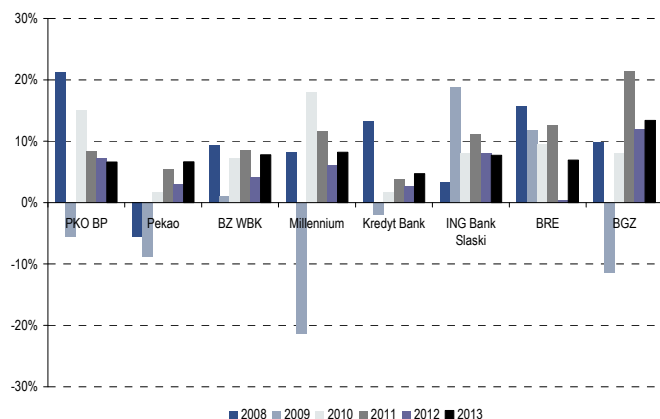
Source: Citi Investment Research and Analysis

Figure 149. Polish Banks – Changes to Administrative Costs Forecasts, 2010-2012 (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	-4,400	-4,400	0.0%	-4,675	-4,675	0.0%	-4,900	-4,900	0.0%
Pekao	-3,767	-3,767	0.0%	-4,003	-4,003	0.0%	-4,128	-4,128	0.0%
BZ WBK	-1,846	-1,846	0.0%	-1,972	-1,972	0.0%	-2,064	-2,064	0.0%
Millennium	-1,134	-1,134	0.0%	-1,210	-1,210	0.0%	-1,259	-1,259	0.0%
Kredyt Bank	-996	-1,046	5.0%	-1,049	-1,118	6.6%	-1,104	-1,176	6.5%
ING Bank Slaski	-1,647	-1,654	0.4%	-1,774	-1,789	0.8%	-1,854	-1,869	0.8%
BRE	-1,734	-1,734	0.0%	-1,907	-1,907	0.0%	-2,000	-2,000	0.0%
BGZ	-956	-974	1.9%	-1,015	-1,057	4.1%	-1,086	-1,130	4.0%
Total	-16,481	-16,556	0.5%	-17,606	-17,731	0.7%	-18,395	-18,525	0.7%

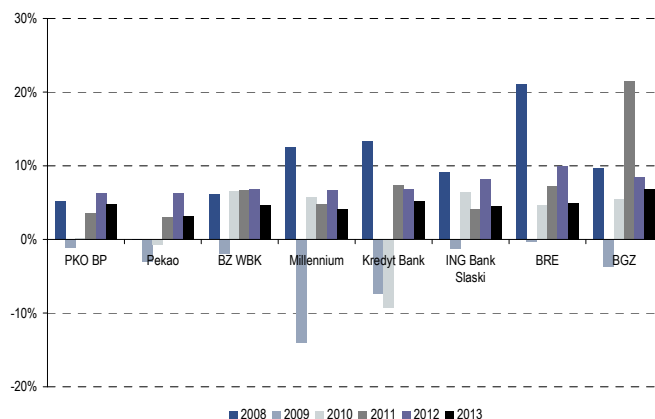
Source: Citi Investment Research and Analysis

Figure 150. Polish Banks – Total Revenues Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 151. Polish Banks – Administrative Costs Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 152. Polish Banks – Changes to Pre-Provision Income Forecasts, 2010-2012 (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	6,656	6,638	-0.3%	7,295	7,161	-1.8%	8,023	7,719	-3.8%
Pekao	3,906	3,906	0.0%	4,439	3,899	-12.2%	5,018	4,301	-14.3%
BZ WBK	1,955	1,942	-0.7%	2,111	1,975	-6.5%	2,406	2,190	-9.0%
Millennium	782	768	-1.8%	959	808	-15.7%	1,086	925	-14.8%
Kredyt Bank	697	654	-6.2%	761	629	-17.3%	897	654	-27.1%
ING Bank Slaski	1,329	1,290	-2.9%	1,446	1,393	-3.7%	1,625	1,558	-4.1%
BRE	1,783	1,783	0.0%	1,913	1,623	-15.1%	2,209	1,774	-19.7%
BGZ	317	227	-28.3%	393	289	-26.5%	521	397	-23.8%
Total	17,425	17,208	-1.2%	19,317	17,778	-8.0%	21,784	19,517	-10.4%

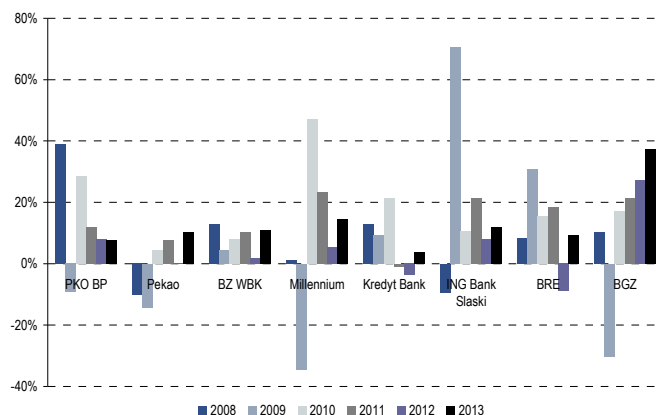
Source: Citi Investment Research and Analysis

Figure 153. Polish Banks – Changes to Provisioning Estimates, 2011E-2013E (Polish Zloty in million)

	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	-1,755	-1,755	0.0%	-1,816	-2,365	30.3%	-2,004	-2,757	37.5%
Pekao	-563	-563	0.0%	-639	-1,073	68.1%	-719	-1,162	61.6%
BZ WBK	-348	-348	0.0%	-313	-503	60.5%	-358	-544	52.2%
Millennium	-180	-184	2.0%	-249	-443	77.6%	-245	-475	94.1%
Kredyt Bank	-338	-286	-15.3%	-378	-514	35.9%	-354	-534	50.8%
ING Bank Slaski	-230	-226	-2.1%	-298	-506	69.7%	-332	-559	68.1%
BRE	-423	-423	0.0%	-562	-862	53.3%	-601	-915	52.4%
BGZ	-190	-142	-25.2%	-167	-216	29.0%	-193	-242	25.7%
Total	-4,027	-3,926	-2.5%	-4,423	-6,482	46.6%	-4,805	-7,188	49.6%

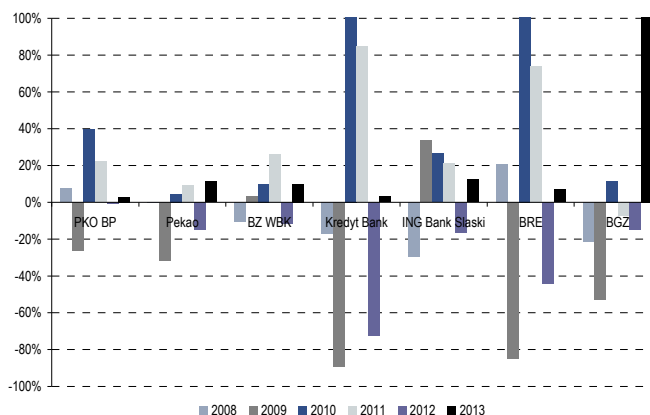
Source: Citi Investment Research and Analysis

Figure 154. Polish Banks – Pre-Provision Income Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 155. Polish Banks – Net Income Growth Rates, 2008-2013E (Percentage)



Source: Company data, CIRA estimates (2011-13)

Figure 156. Polish Banks – Changes in Net Profit Forecasts, 2011E-2013E (Polish Zloty in million)

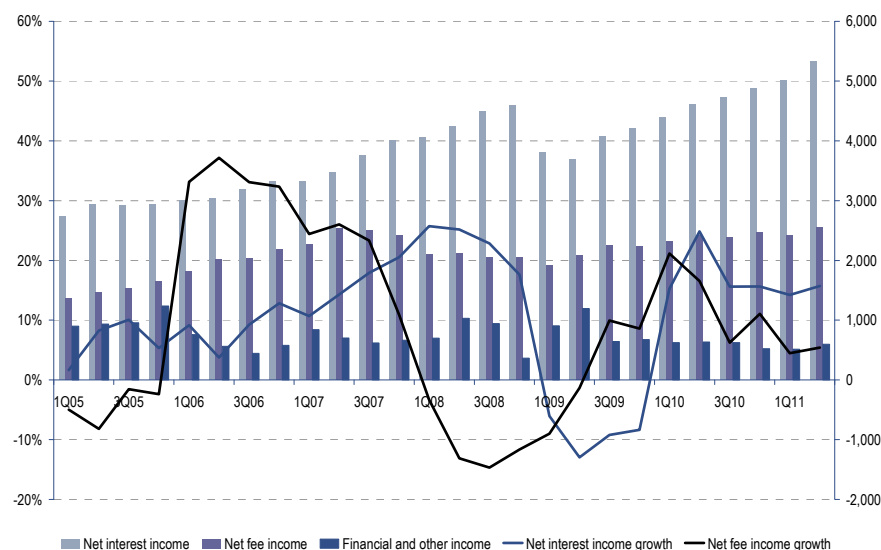
	2011E			2012E			2013E		
	OLD	NEW	Chg.	OLD	NEW	Chg.	OLD	NEW	Chg.
PKO BP	3,940	3,926	-0.4%	4,446	3,892	-12.5%	4,856	4,005	-17.5%
Pekao	2,761	2,761	0.0%	3,133	2,344	-25.2%	3,552	2,612	-26.5%
BZ WBK	1,229	1,218	-0.9%	1,336	1,079	-19.3%	1,504	1,186	-21.1%
Millennium	476	462	-3.0%	567	292	-48.5%	673	360	-46.5%
Kredyt Bank	343	342	-0.3%	310	94	-69.8%	439	97	-78.0%
ING Bank Slaski	914	886	-3.0%	952	740	-22.3%	1,070	832	-22.2%
BRE	1,117	1,117	0.0%	1,060	624	-41.2%	1,267	667	-47.3%
BGZ	104	69	-33.5%	183	59	-67.7%	262	124	-52.9%
Total	10,780	10,712	-0.6%	11,804	9,064	-23.2%	13,360	9,758	-27.0%

Source: Citi Investment Research and Analysis

Appendix – 2Q11 Results Illustrated

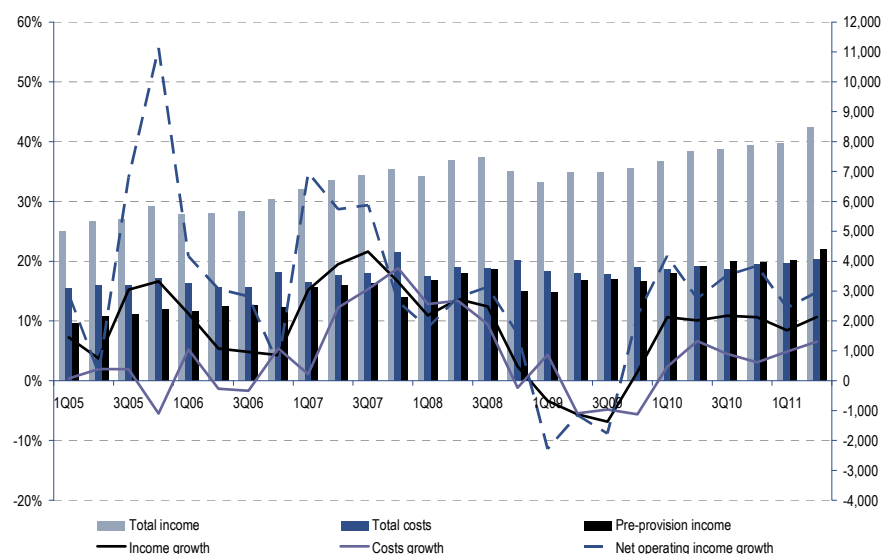
Financial Results of CIRA Universe

Figure 157. Polish Banks – Revenues Trend, 1Q05-2Q11 (Polish Zloty in million)



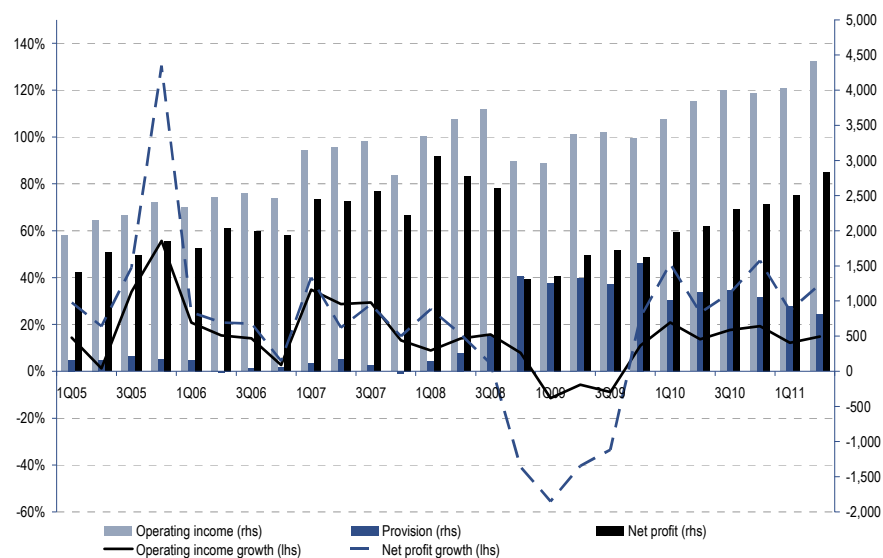
Source: Company reports, Citi Investment Research and Analysis

Figure 158. Polish Banks – Revenues, Costs and Pre-Provision Profit Trends, 1Q05-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

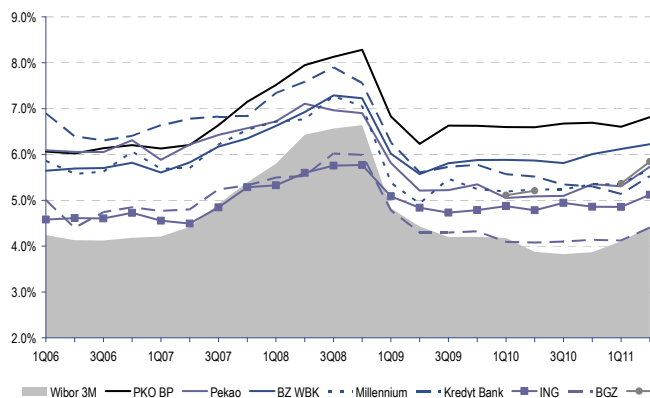
Figure 159. Polish Banks – Pre-Provision Profits, Provision and Net Income Trends, 1Q05-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

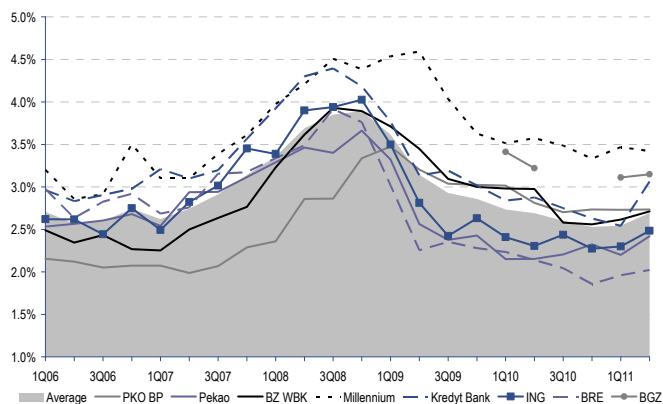
Profitability and Main Ratios

Figure 160. Polish Banks – Yield on Assets, 1Q06-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Figure 161. Polish Banks – Cost of Funding, 1Q06-2Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

Figure 162. Polish Banks – Net Profit, 1Q07-2Q11 (Polish Zloty in million)

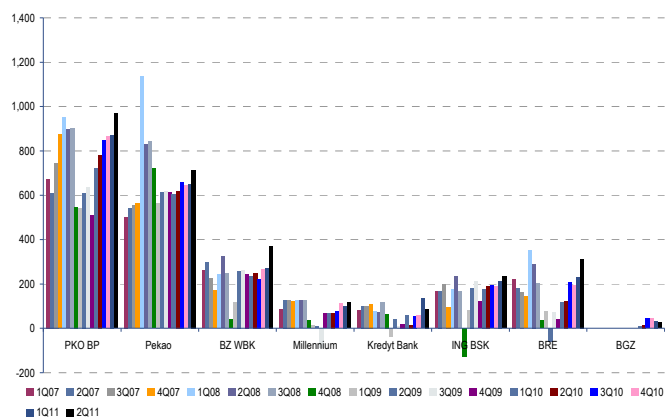
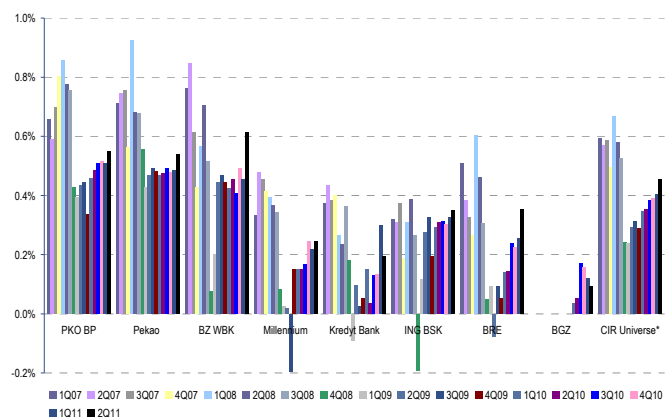
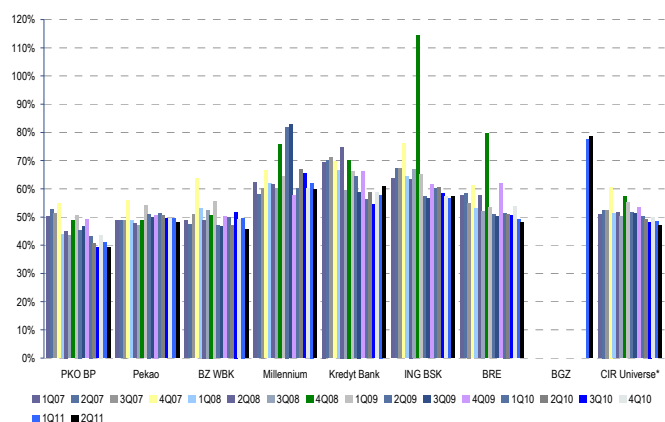


Figure 164. Polish Banks – ROA, 1Q07-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 166. Polish Banks – Cost-to-Income, 1Q07-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 163. Polish Banks – ROE, 1Q07-2Q11 (Percentage)

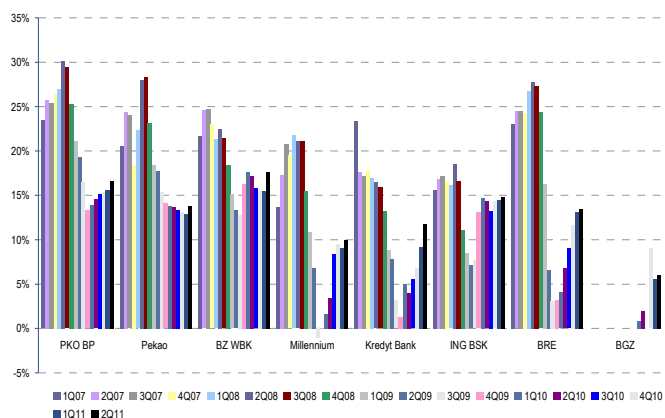
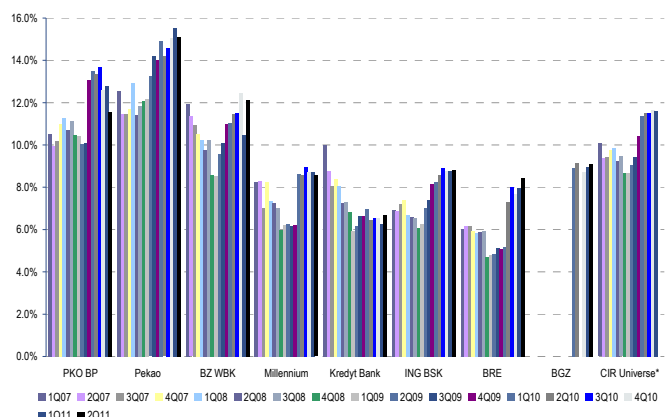
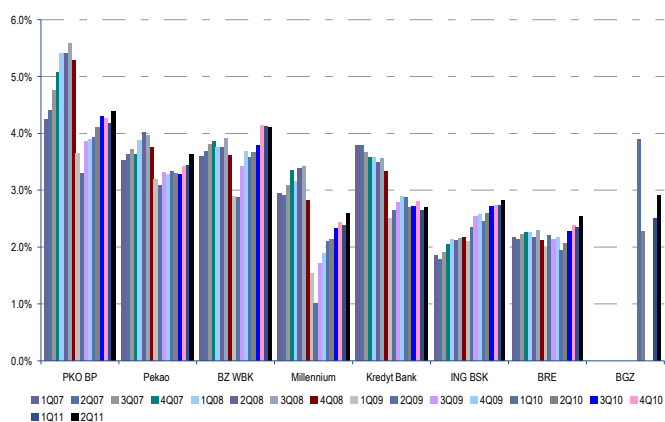


Figure 165. Polish Banks – Equity-to-Assets, 1Q07-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 167. Polish Banks – NIM at Interest-Bearing Assets, 1Q07-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Lending

Figure 168. Polish Banks – Loan Growth Rates, Jan 98 - Jun 11 (Percentage)

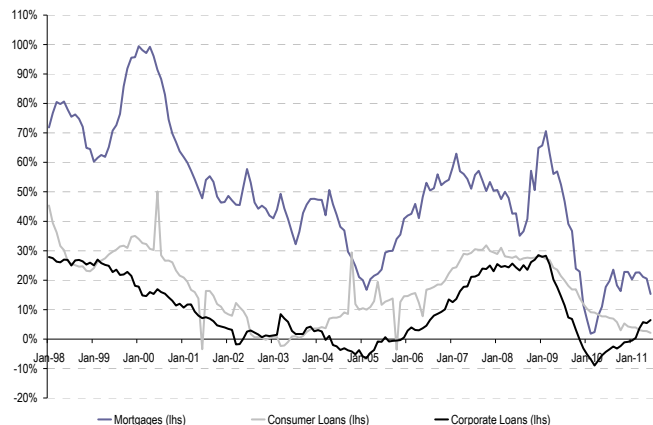


Figure 170. Polish Banks – Loan-to-Assets and Loan-to-Deposits, 2Q10 (Percentage)

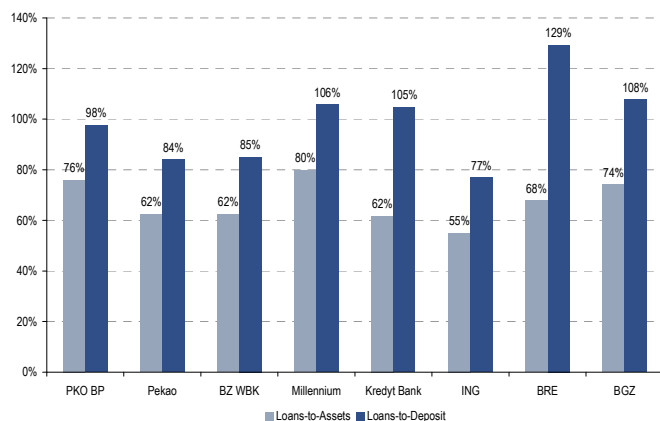


Figure 172. Polish Banks – Mortgage Loans, 1Q11 (Polish Zloty in million)

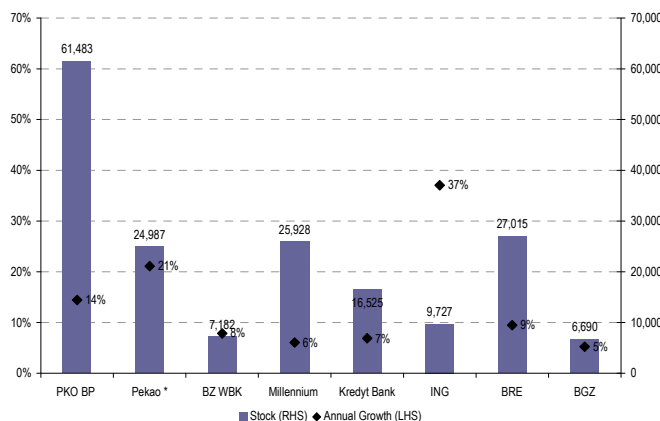


Figure 169. Polish Banks – Quarterly Change in Loans, 2Q11 (Percentage)

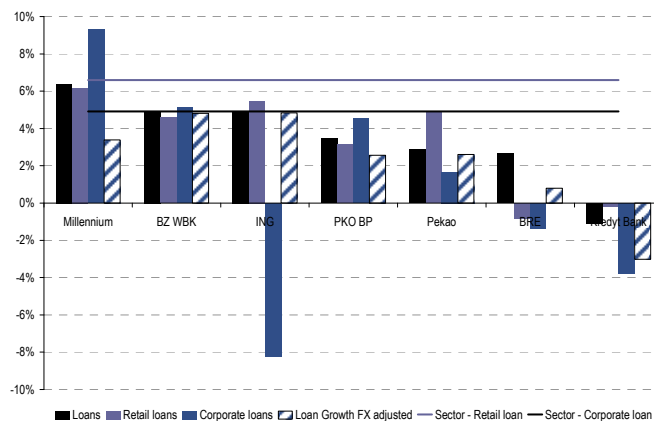


Figure 171. Polish Banks – Corporate Loans, 2Q11 (Polish Zloty in million)

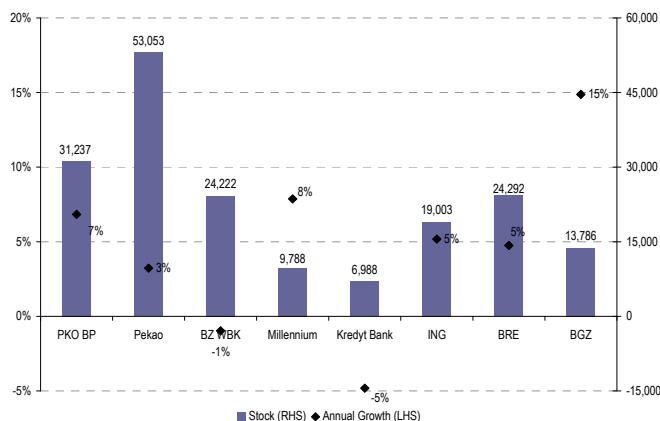
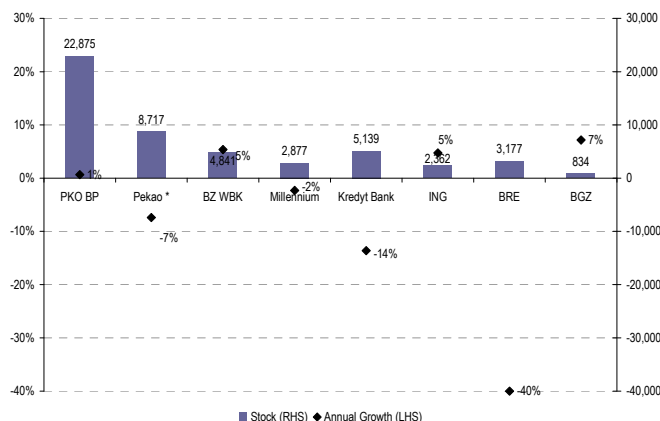


Figure 173. Polish Banks – Retail Loans Excl. Mortgage, 2Q11 (Polish Zloty in million)



Source for all: Company reports, Citi Investment Research and Analysis

Deposits and AUM

Figure 174. Polish Banks – Funding Structure, 2Q11 (Percentage)

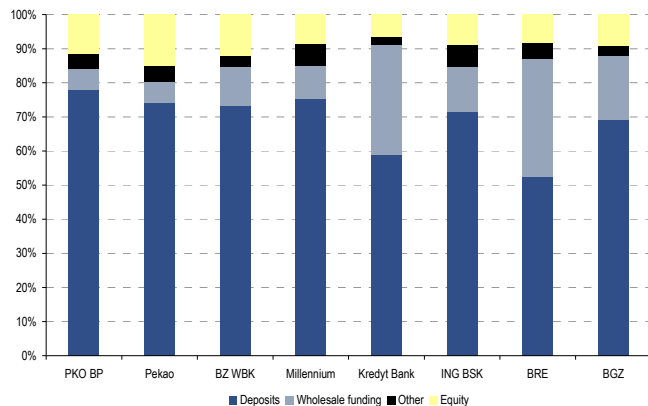


Figure 175. Polish Banks – Quarterly Change in Deposits, 2Q11 (Percentage)

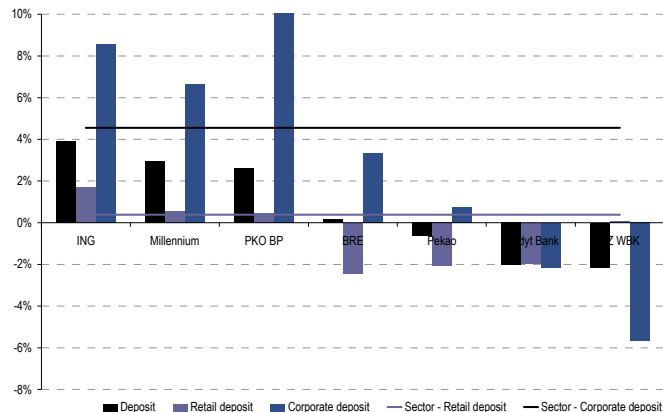


Figure 176. Polish Banks – Retail Deposits, 2Q11 (Polish Zloty in million)

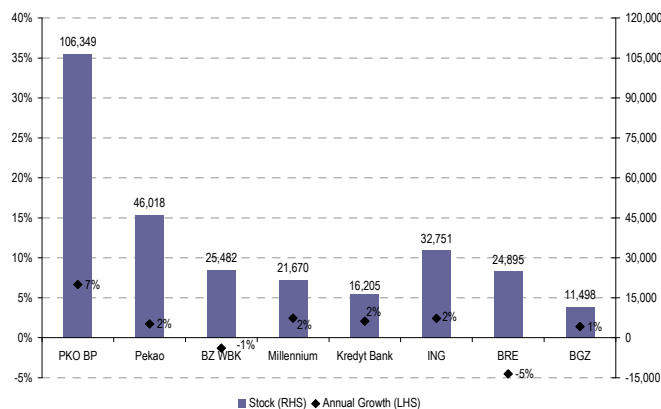


Figure 177. Polish Banks – Corporate Deposits, 2Q11 (Polish Zloty in million)

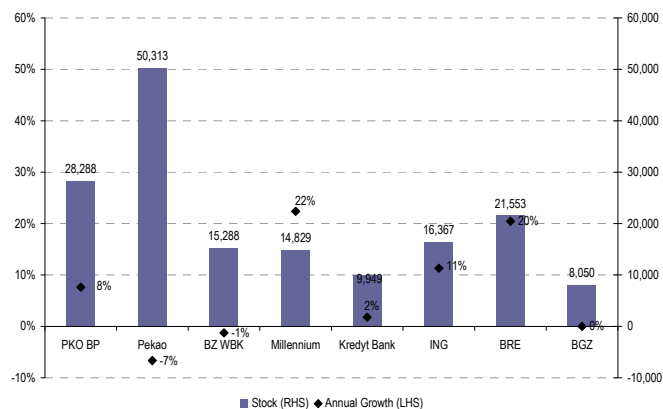


Figure 178. Polish Banks – Total Funds, 2Q11 (Polish Zloty in million)

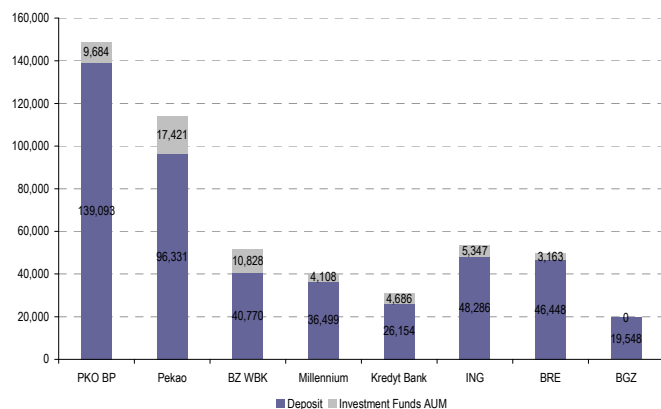
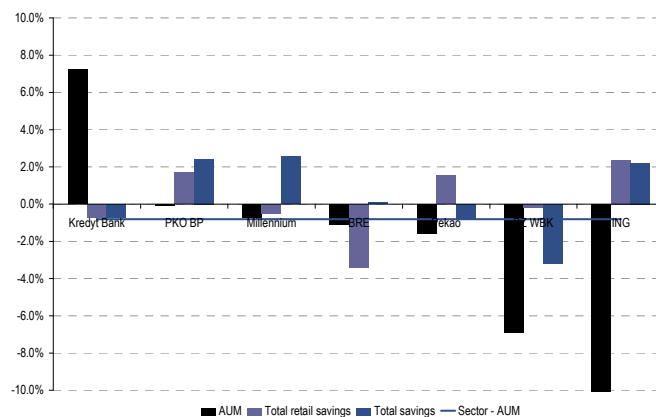


Figure 179. Polish Banks – Quarterly Change in Total Funds, 2Q11 (Percentage)



Source for all: Company reports, Citi Investment Research and Analysis

Revenues

Figure 180. Polish Banks – Net Interest Income, 1Q07-2Q11 (Polish Zloty in million)

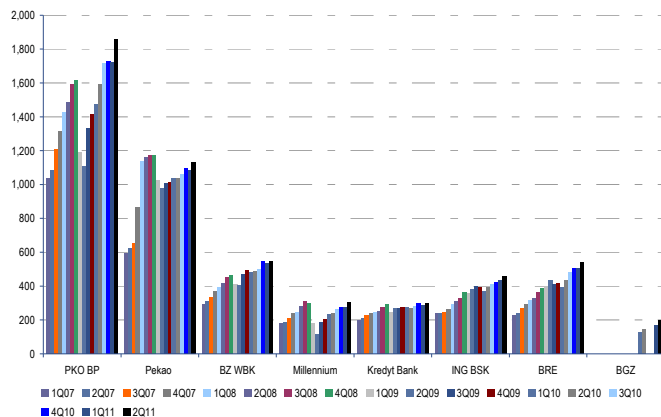


Figure 182. Polish Banks – Net Fee, 1Q07-2Q11 (Polish Zloty in million)

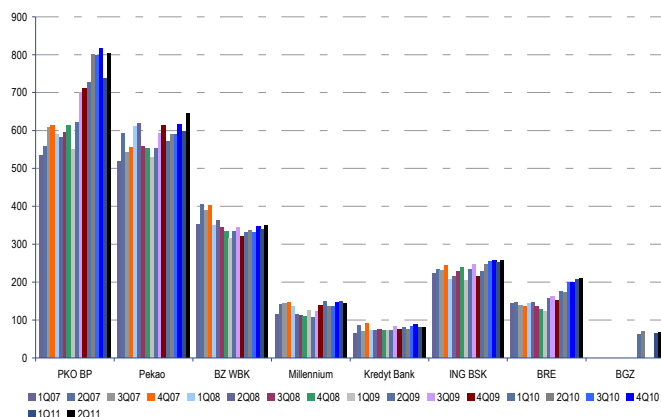


Figure 184. Polish Banks – Other and Financial Income, 1Q07-2Q11 (Polish Zloty in million)

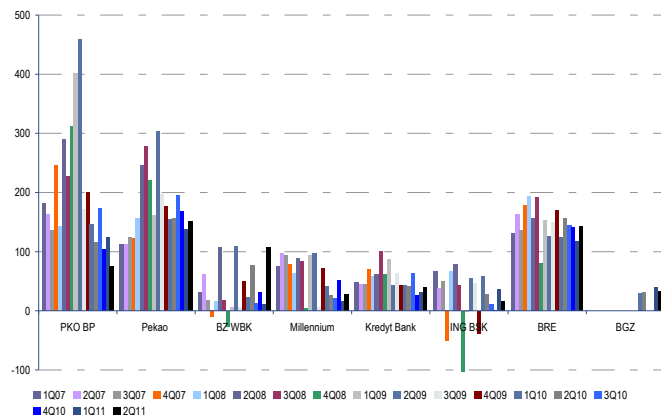


Figure 181. Polish Banks – Annual Change in Net Interest Income, 1Q07-2Q11 (Percentage)

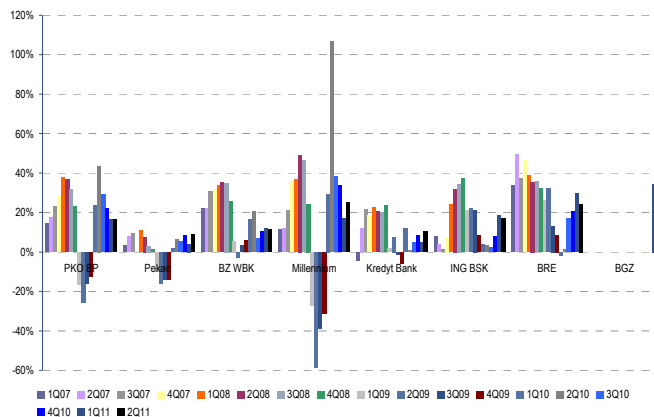


Figure 183. Polish Banks – Annual Change in Net Fees, 1Q07-2Q11 (Percentage)

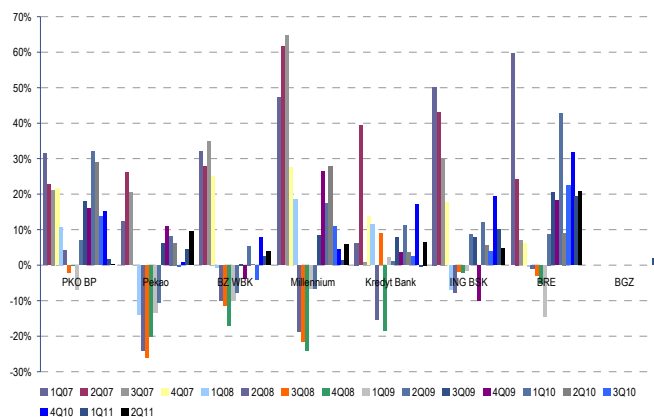
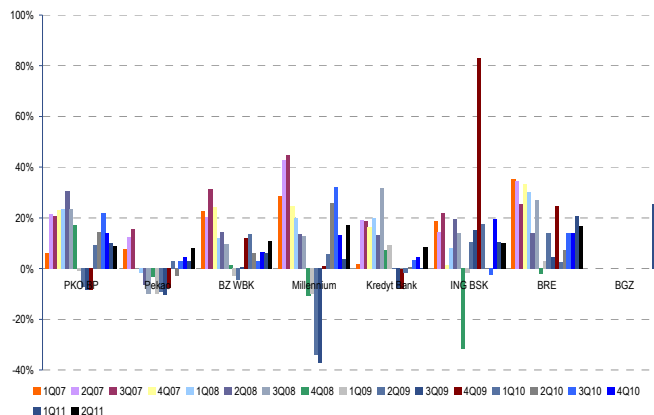


Figure 185. Polish Banks – Annual Change in Total Income, 1Q07-2Q11 (Percentage)



Source for all: Company reports, Citi Investment Research and Analysis

Administrative Costs And Pre-Provision Income

Figure 186. Polish Banks – Administrative Costs, 1Q07-2Q11 (Polish Zloty in million)

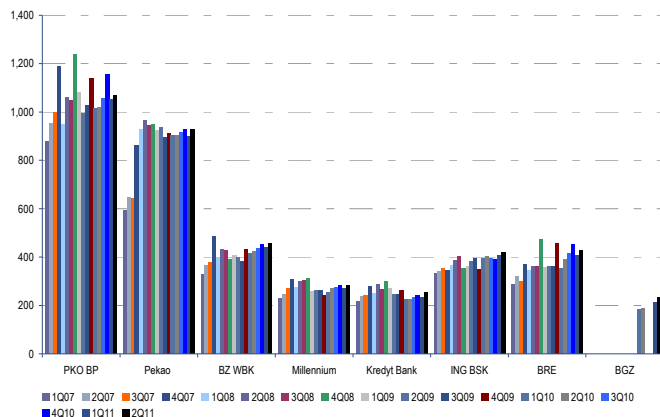


Figure 188. Polish Banks – Pre-Provision Income, 1Q07-2Q11 (Polish Zloty in million)

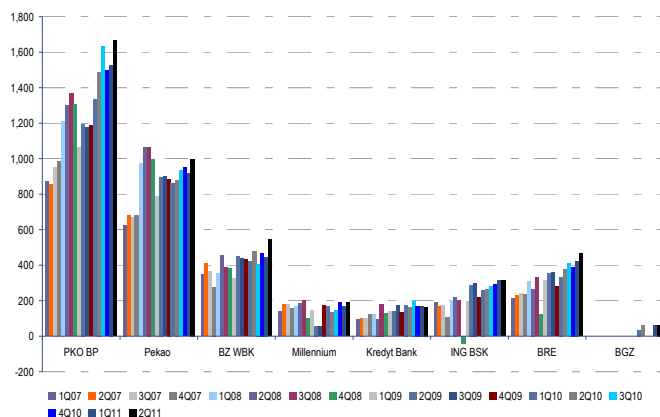


Figure 190. Polish Banks – Revenues-to-Assets, 1Q07-2Q11 (Percentage)

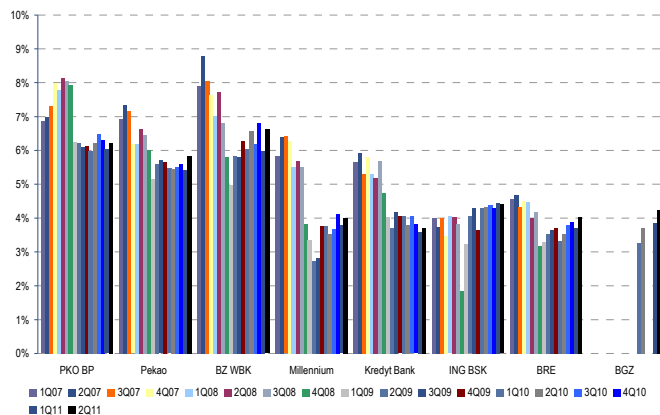


Figure 187. Polish Banks – Annual Change in Costs, 1Q07-2Q11 (Percentage)

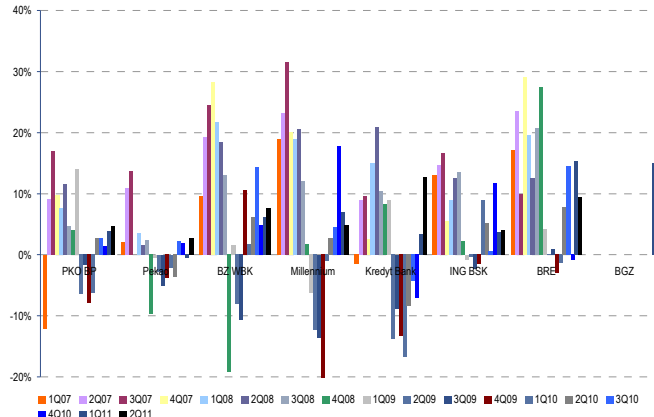


Figure 189. Polish Banks – Annual Change in Pre-Provision Income, 1Q07-2Q11 (Percentage)

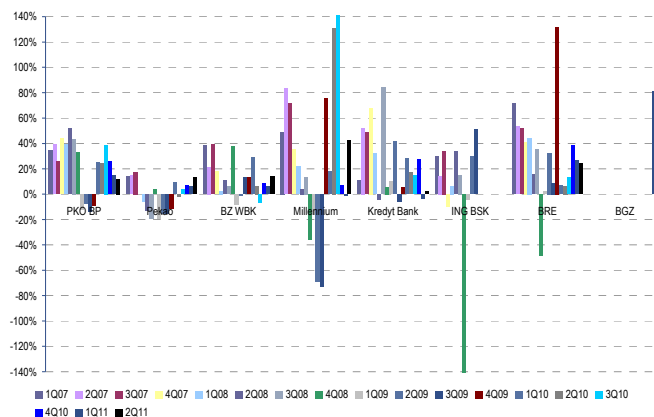
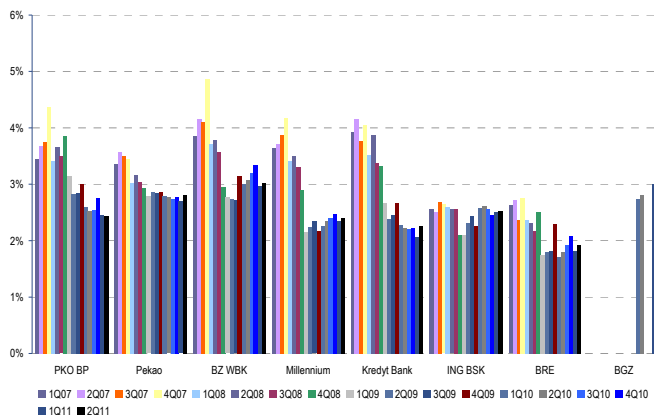


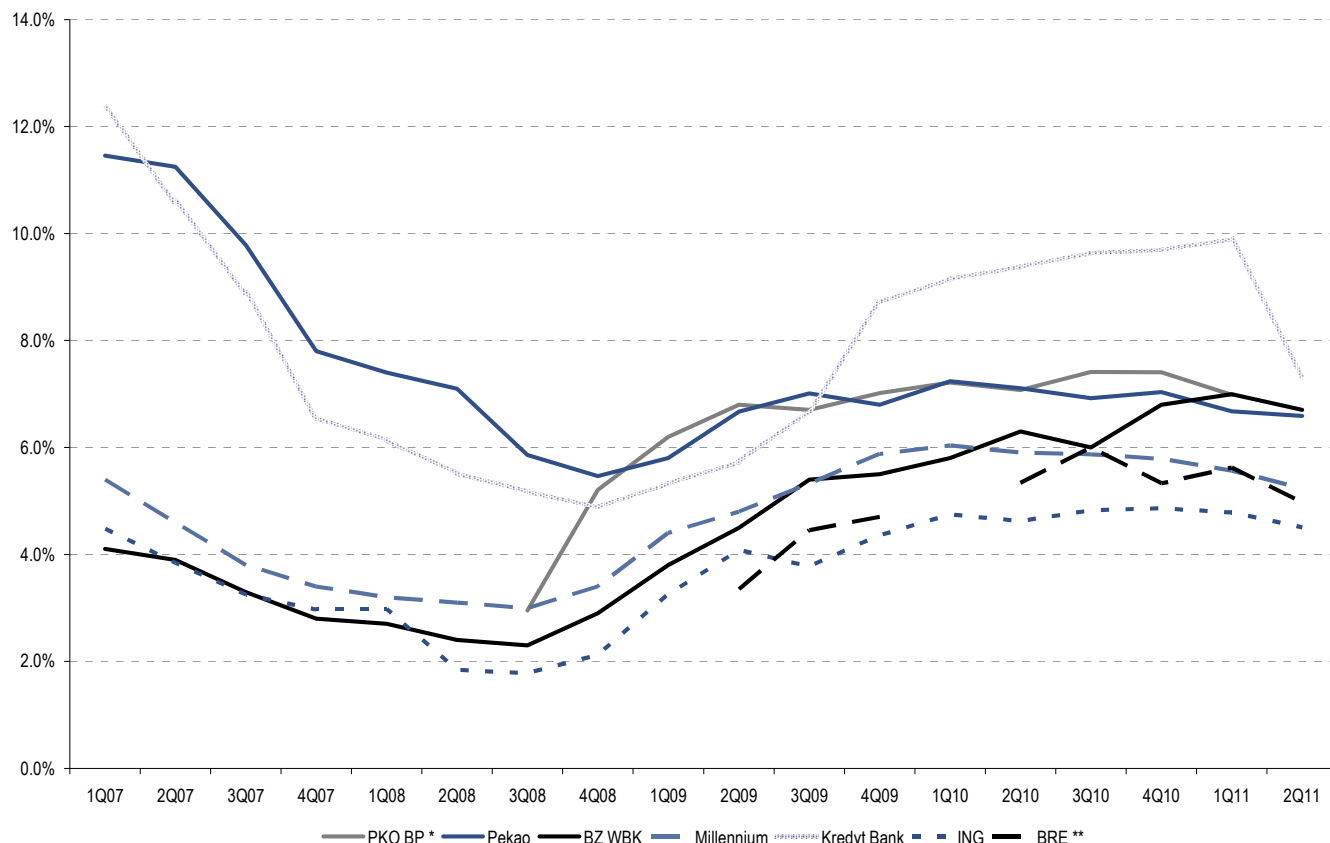
Figure 191. Polish Banks – Costs-to-Assets, 1Q07-2Q11 (Percentage)



Source for all: Company reports, Citi Investment Research and Analysis

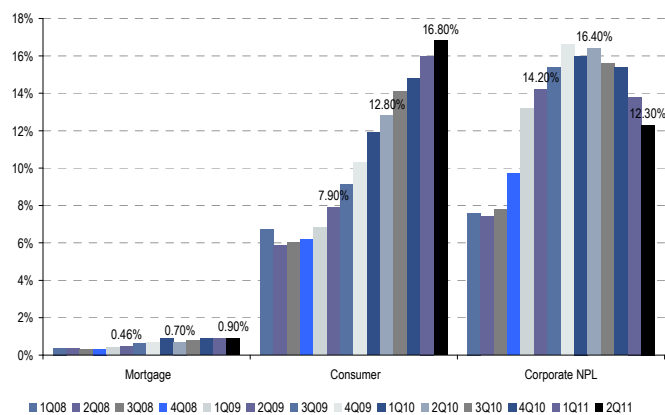
NPL Ratios

Figure 192. Polish Banks – NPL Ratios, 1Q07-2Q11 (Percentage)



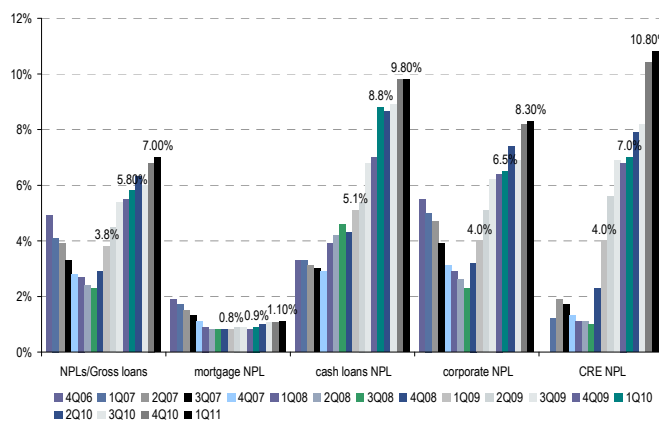
Source: Company reports, Citi Investment Research and Analysis

Figure 193. Bank Millennium – NPL Ratios, 1Q08-2Q11 (Percentage)



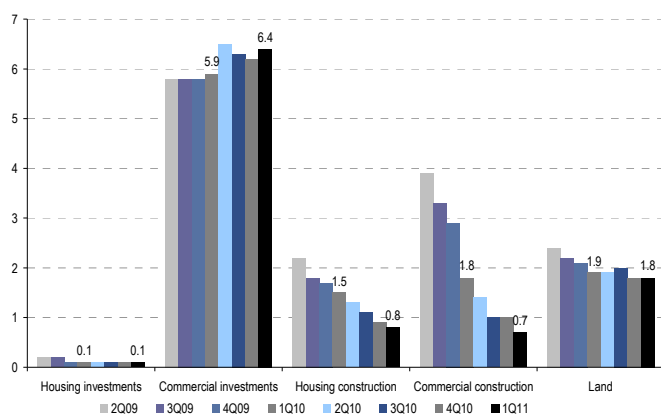
Source: Company reports, Citi Investment Research and Analysis

Figure 194. BZ WBK – NPL Ratios, 4Q06-1Q11 (Percentage)



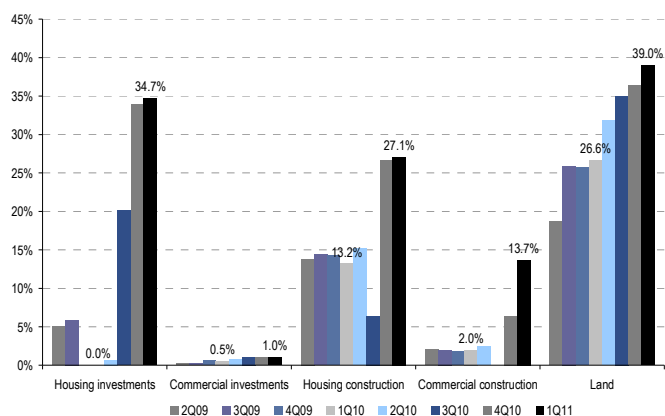
Source: Company reports, Citi Investment Research and Analysis

Figure 195. BZ WBK – CRE Loans, 2Q09-1Q11 (Polish Zloty in billion)



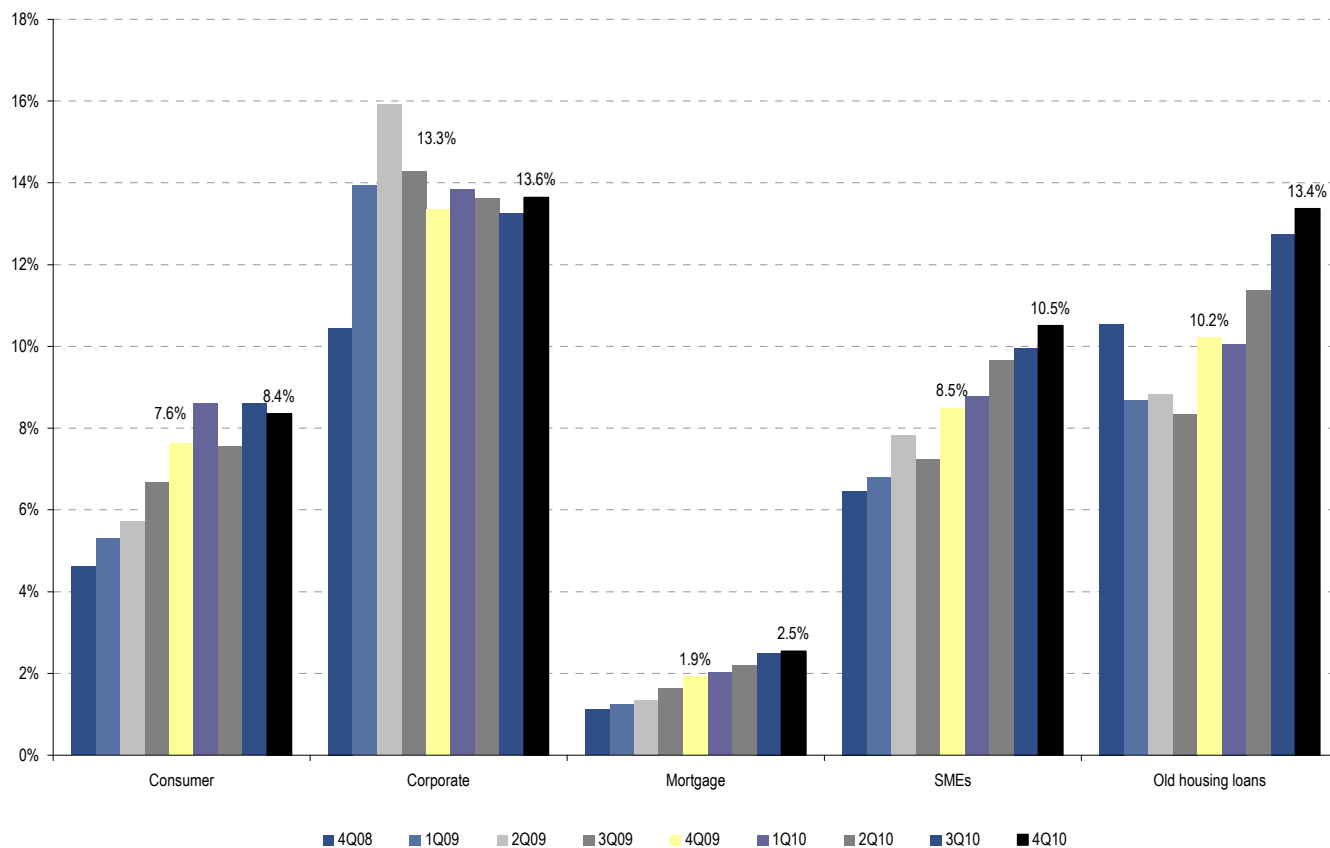
Source: Company reports, Citi Investment Research and Analysis

Figure 196. BZ WBK – NPL Ratio in CRE Loans, 2Q09-1Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

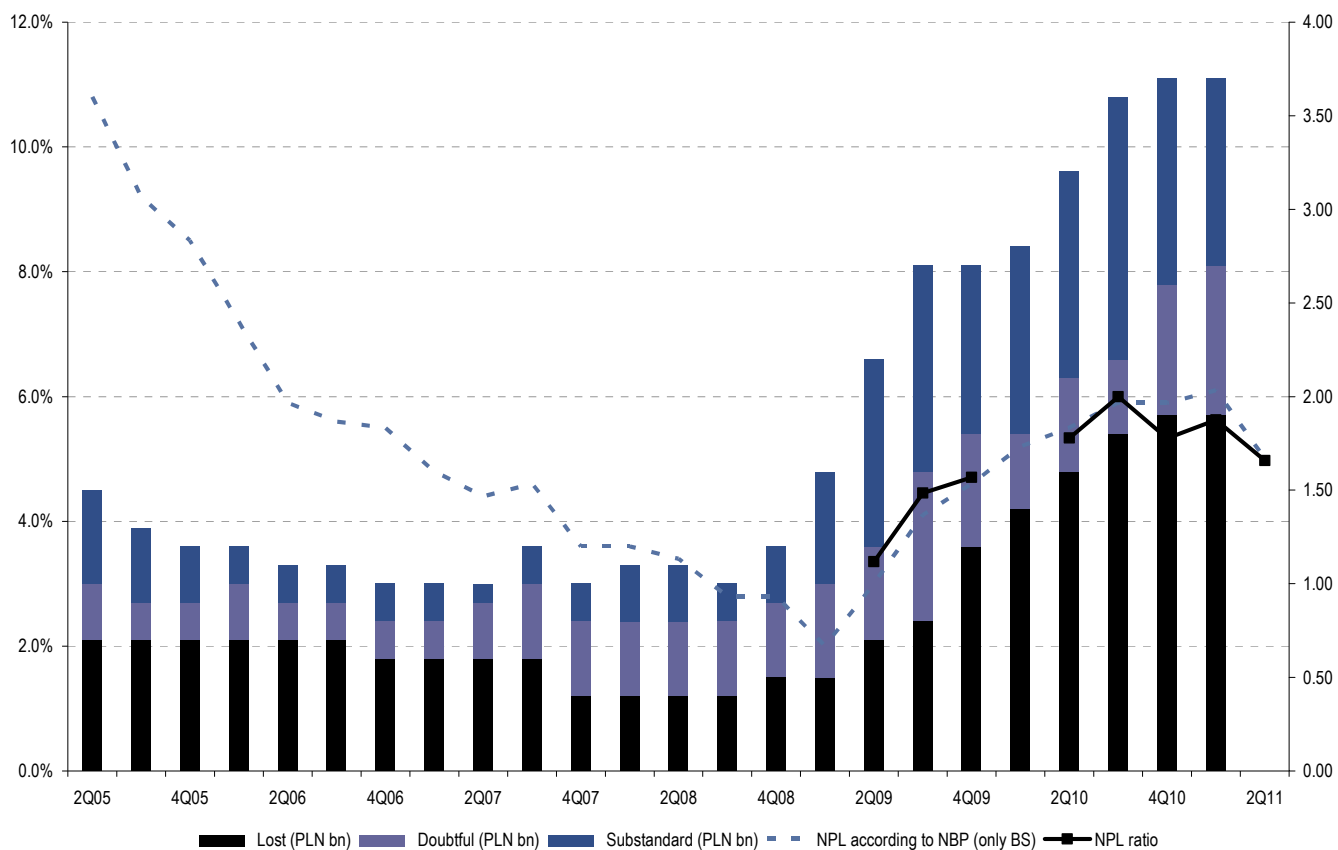
Figure 197. PKO BP – NPL Ratios*, 4Q08-4Q10 (Percentage)



Note: * Share of loans with recognised losses in total loans (unconsolidated)

Source: Company reports, Citi Investment Research and Analysis

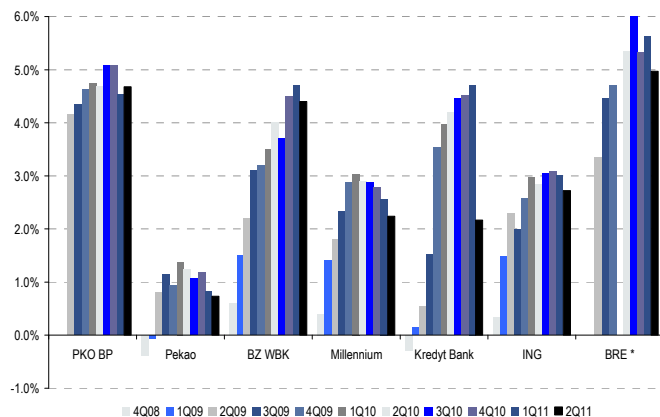
Figure 198. BRE Bank – Default Ratio and NPL Ratios According to NBP Classification, 2Q05-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

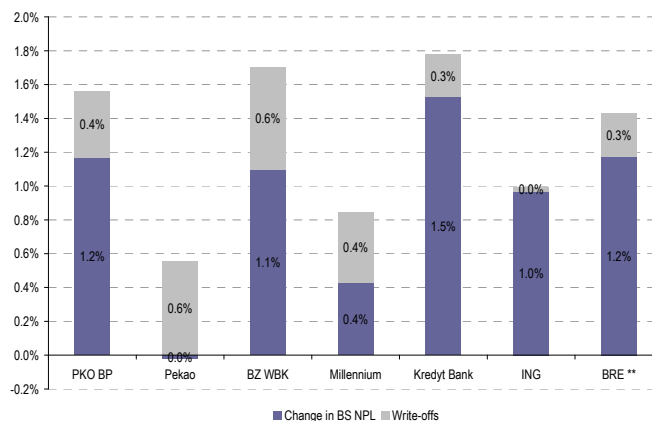
NPL Formation

Figure 199. Polish Banks – Accumulated Balance Sheet NPL Formation Since 3Q08, 4Q08-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

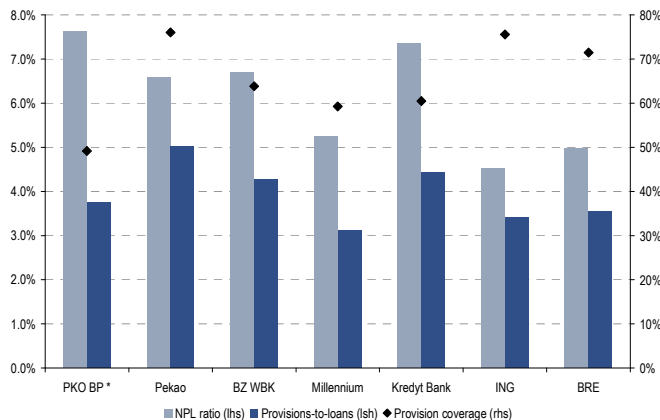
Figure 200. Polish Banks – Total NPL Formation as % of 2010 Loans, 2010 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

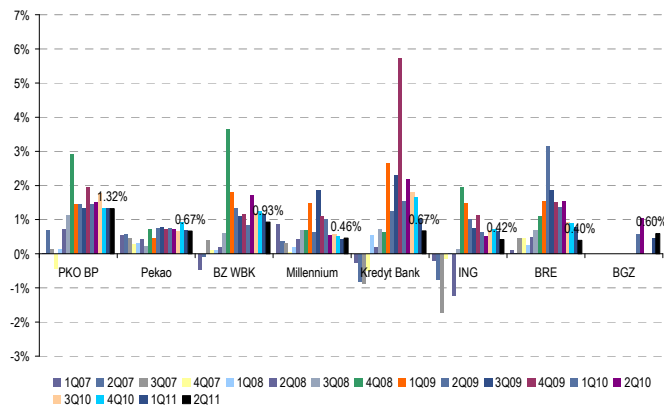
Provisioning

Figure 201. Polish Banks – Summary of Provision and NPL, 2Q11 (Percentage)



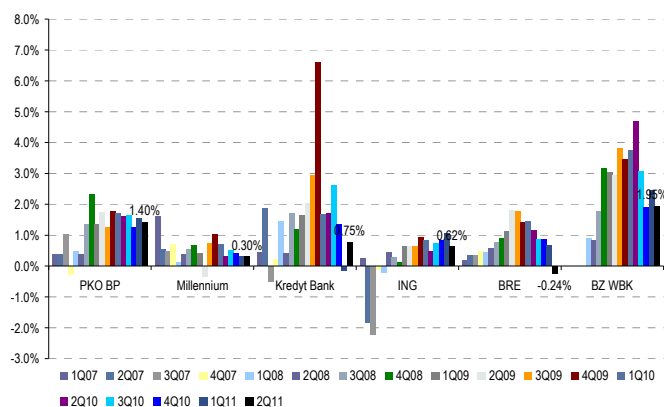
Source: Company reports, Citi Investment Research and Analysis

Figure 202. Polish Banks – Provision Charges on Total Loans, 1Q07-2Q11 (Percentage)



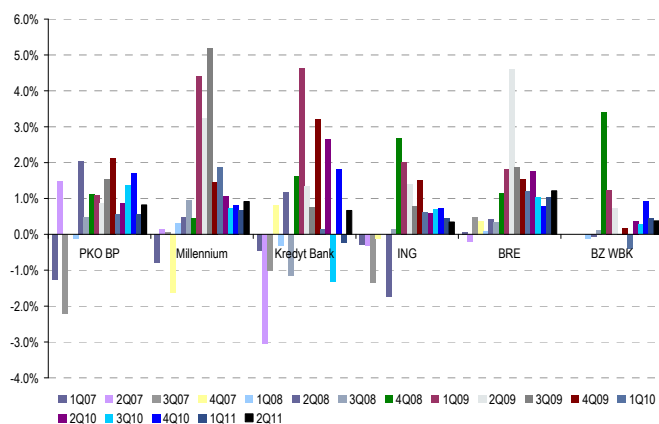
Source: Company reports, Citi Investment Research and Analysis

Figure 203. Polish Banks – Provision Charges on Retail Loans, 1Q07-2Q11 (Percentage)



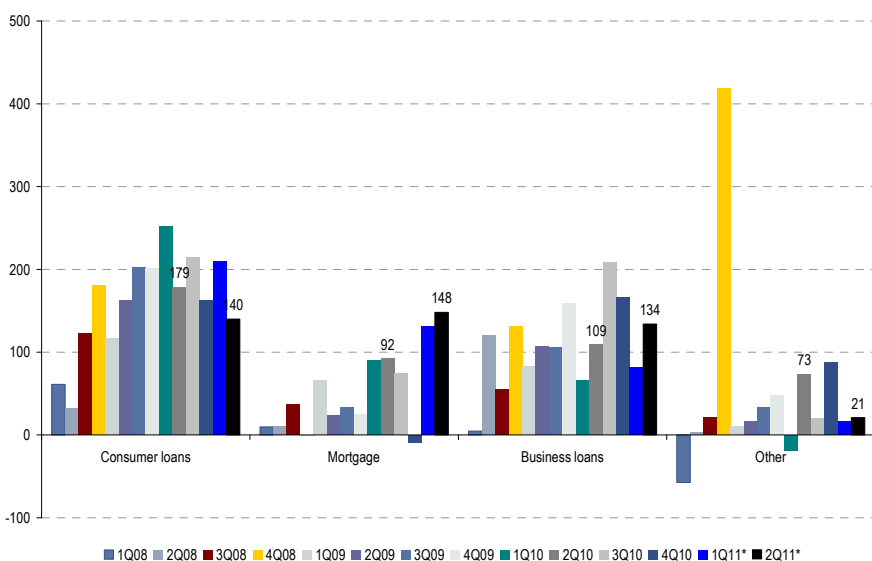
Source: Company reports, Citi Investment Research and Analysis

Figure 204. Polish Banks – Provision Charges on Corporate Loans, 1Q07-2Q11 (Percentage)



Source: Company reports, Citi Investment Research and Analysis

Figure 205. PKO BP – Provisioning Per Product (Unconsolidated), 1Q08-1Q11 (Polish Zloty in million)



Source: Company reports, Citi Investment Research and Analysis

* consolidated data

PKO BP

Company description

PKO BP is Poland's largest bank, with c1,250 branches. It has approximately 12% market share of total banking assets and is particularly dominant in retail banking with c.27% retail deposit market share and c35% mortgage lending market share. PKO BP is 51% owned (directly and through state-controlled bank BGK) by the Polish state.

Investment strategy

We like the bank's strategy to base the growth of the business on growing lending coupled with its strong retail franchise, giving it the access to relatively cheap and stable funding. We note, however, that in the short term the aggressive lending strategy may lead to high provisioning but we view that risk as more than priced in. We rate the stock Buy.

Valuation

Our Standard Warranted Equity Valuation of ZI 41.0 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. Our sustainable ROE estimate is 17%. We use a cost of equity of 11% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 47.1 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). We set our target price at ZI 41.0 using the more conservative short-term approach.

Risks

The strong capital position coupled with the strongest retail franchise and implicit State Treasury support justify a Low Risk rating, in our opinion. The following risk factors might impede the share price from reaching our target price. The macro economy may perform better or worse than anticipated and lead to higher or lower provisioning and slower or higher loan growth than anticipated. Specific to the bank: 1) state ownership may constrain management's ability to restructure the business, particularly its ability to decrease employee levels, and impact the bank's capitalisation; 2) the bank was active in extending FX-denominated loans to retail customers, who could face repayment difficulties; and 3) margin developments have been volatile recently and future margin development could be better or worse than we expect.

Bank Pekao SA

Company description

Bank Pekao is now Poland's second-largest bank following the acquisition of the majority of the business of BPH Bank (referred to as 'BPH-285' in reference to the 285 branches involved in the transaction). The merger was triggered by the acquisition of HVB (BPH's majority shareholder) by Unicredit, which owned a 52.9% stake in Bank Pekao prior to the merger. Unicredit now owns a 59.4% stake in the combined entity. The combined entity has c.12% asset market share, 1,058 outlets, and serves c.5m customers.

Investment strategy

Bank Pekao continues to enjoy high liquidity and a solid capital base. Thanks to that it is well positioned to take advantage from potential M&A opportunities and benefit from expected rebound in corporate lending (especially in lending to the biggest corporate clients). This potential is, in our opinion, not reflected in the market price and thus we rate the stock Buy.

Valuation

Our Standard Warranted Equity Valuation of ZI 150 per share is based on the formula: $\text{Price} / \text{Book value} = (\text{Sustainable ROE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. We assume sustainable return on equity of 16.0%, a sustainable growth rate of 5.0% and a cost of equity of 10.5%. Given the bank's overcapitalization (Tier 1 at 18.3%), we value the bank also on the capital-adjusted base and assuming capital normalised ROE of 21% we arrive at fair value of ZI 192 per share. Our Economic Value Added Valuation of ZI 168 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). We set our target price using average of the more short-term approach and capital-adjusted base at ZI 171.

Risks

We rate Bank Pekao Low Risk because the bank's management and its strategic shareholder are conservative and more risk-averse than their peers. This was made apparent by the decision of the bank to exit the FX mortgage lending market several years ago. Specifically for Bank Pekao, we highlight that: 1) the bank's conservative risk and capital management may lead to lower lending growth and dividend payment than we anticipate 2) provisioning, low in the last slowdown (2009) could surprise negatively in the next slowdown/recession period due to lower buffer of over-provisioning. These risk factors could cause the share price to deviate significantly from our target price.

BRE Bank SA

Company description

BRE Bank (70% owned by Commerzbank) is the third-largest Polish bank, with a market share of approximately 8% of banking assets. Historically, it has focused on commercial banking, although since 2001 it has been expanding its retail business, from 8% of its lending in 2000 to 50% in 2008.

Investment strategy

While a sharp increase in loan loss provisioning weighed on profitability in 2009-10 we forecast a recovery in profitability driven by significantly lower provisioning over the next couple of years, coupled with continued efforts to increase the bank's fee generation, both from retail and corporate business. Additionally, the bank should no longer be constrained by its weak capital position following a completed ZI 2bn capital increase in 2010. We rate the bank Buy.

Valuation

Our Standard Warranted Equity Valuation of ZI 298 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. We assume a sustainable return on equity of 15.0%, a cost of equity of 11.0% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 296 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital, assuming no capital increase) and the proposed value of capital increase. In line with the approach we adopt for the rest of our coverage universe, our target price is based upon the shorter-term approach, and is set at ZI 298.

Risks

We rate BRE Bank Medium Risk based on our assessment of industry- and company-specific risk factors. The following risk factors might cause the share price to deviate from our target price. The macro economy may perform worse or better than anticipated and lead to higher/lower provisioning and slower/faster loan growth than anticipated. Specifically for BRE Bank, we highlight that: 1) the bank's loan book is heavily weighted towards FX mortgage loans and a weaker zloty could negatively impact asset quality; and 2) the bank remains highly dependent on funding from parent Commerzbank, which could constrain the bank's growth outlook unless the operating environment improves dramatically. If the impact on the company from any of these factors proves to be more negative than we anticipate, the stock will likely have difficulty achieving our financial and price targets. Likewise, if any of these factors proves to have less of an effect than we anticipate, the stock could materially outperform our target.

ING Bank Slaski SA

Company description

ING Bank Slaski is Poland's fourth-largest bank by assets, with a market share of approximately 6%. It is a universal bank and has been operating since 1989. The bank is particularly strong in southern Poland, but is present nationwide. ING Bank NV holds a 75% stake in ING Bank Slaski. The bank co-operates closely with ING Group's investment management, life insurance and pension fund businesses in Poland.

Investment strategy

With the lowest loan-to-deposit ratio in CIRA's CEEMEA universe and the third-largest retail deposit base in the sector, the bank has been particularly well positioned to benefit from the current environment where most banks were more focused on liquidity rather than on growing balance sheets. This advantage has been reflected in recent financial results, which have been marked by impressive margin expansion. Thus we rate the shares Buy.

Valuation

Our Standard Warranted Equity Valuation of ZI 886 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$.

Given higher regulatory charges, we set our assumption of sustainable ROE at 14.5% and use a cost of equity of 10.5% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 1,007 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). Given the concern with the outlook for global growth, we set our target price using the more conservative short-term approach at ZI 886.

Risks

We rate ING Bank Slaski Medium Risk after assessing industry- and company-specific risks that may affect the achievement of our target price. The following risk factors might cause the share price to deviate from our target price. The macro economy may perform better or worse than anticipated and lead to higher or lower provisioning and slower or higher loan growth than anticipated. Specifically for ING Bank Slaski, we highlight: (1) that despite the bank's strong liquidity its net interest margin may be more negatively affected by increased competition for deposits than we expect; and (2) the upside risk that profitability may recover to normalised sector levels, prompting a further re-rating. If the impact on the company from any of these factors proves to be more positive than we anticipate, the stock may outperform our financial and price targets.

Bank Zachodni WBK

Company description

Bank Zachodni WBK SA is Poland's sixth-largest bank by assets, with a market share of 5%. It has historically focused on servicing medium-sized companies and retail clients. Allied Irish Banks PLC recently sold its 70.5% strategic stake in Bank Zachodni WBK to Santander.

Investment strategy

We like BZ WBK's income diversification but note the bank's continued weakness in investment fund business, in the past being one of the core businesses for the bank. We still wait for visible changes implemented by the new strategic investor (Santander). In our opinion, the bank's interesting business model is fully priced in and we rate the shares Hold.

Valuation

Our Standard Warranted Equity Valuation of ZI 239 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. We set our assumption of sustainable ROE at 18.0% and use a cost of equity of 10.5% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 271 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). Given the concern with the outlook for global growth, we set our target price using the more conservative short-term approach at ZI 239.

Risks

We rate Bank Zachodni WBK Medium Risk after assessing industry- and company-specific risks that may affect the achievement of our target price. Risks to the Polish banking market include: (1) the possibility of adverse movements in interest rates and bond yields, which could affect earnings; and (2) the macro economy may perform better or worse than anticipated and lead to higher or lower provisioning and slower or higher loan growth than anticipated. Specifically for Bank Zachodni WBK, we highlight: (1) the bank's large exposure to the real estate and construction sectors; (2) that earnings are sensitive to mutual fund inflows/outflows and the financial results of the bank may be better or worse than our forecasts depending on the development of the bank's mutual fund business.

Bank Millennium SA

Company description

Bank Millennium, majority owned by Banco Comercial Portugues, is a medium-sized Polish bank with over 1 million customers and a strong market position in retail mortgage loans, credit cards and leasing services.

Investment strategy

Over the past several years, Bank Millennium has built a strong position in CHF-denominated mortgage lending, increased the sale of consumer finance products and developed a successful customer deposit collection franchise. In 4Q08, Millennium's CHF mortgage business model collapsed as a result of decreased availability of FX swaps and significantly rising FX swap costs. As a result, we anticipate that the profitability of the bank will be seriously impaired by an increase in the cost of funding. We are sceptical as to whether the strategy of diversification will enable the bank to achieve a 15% ROE in 2012. We rate the shares Sell.

Valuation

Our Standard Warranted Equity Valuation of ZI 4.53 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. We assume a sustainable ROE of 13.5% and use a cost of equity of 11.5% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 4.39 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). In line with the approach we adopt for the rest of our coverage universe, our target price is based upon the shorter-term approach at ZI 4.53.

Risks

We rate Bank Millennium Medium Risk based on our assessment of industry- and company-specific risk factors. The economy may perform better or worse than anticipated and lead to higher or lower provisioning and slower or higher loan growth than anticipated. Additionally, the Polish banking market is rather fragmented and increased competition could put more pressure on margins and earnings than currently expected. Specifically for Bank Millennium: (1) it is more dependent on wholesale funding than its Polish peers, leaving it exposed to higher funding costs; and (2) the bank is the most exposed in our Polish banking coverage universe to CHF-denominated mortgages and thus vulnerable to continued zloty weakness. If the impact of these risk factors is less negative than we currently anticipate, then the stock could materially outperform our target price.

Kredyt Bank SA

Company description

Kredyt Bank, 80% owned by KBC Group, is Poland's eighth-largest bank by assets. The bank has adopted KBC's bancassurance strategy and works in close co-operation with Warta, Poland's second-largest general insurance company, which is wholly owned by the KBC Group.

Investment strategy

In recent years, Kredyt Bank has significantly improved its business model in retail banking, which has led to strong sales of consumer and mortgage loans, but this has not been followed by rising profitability. Recently, management has begun to implement a restructuring plan, achieved significant cost reduction and sold subsidiary Zagiel. In our opinion, the stock price more than reflects the improvement in the bank's performance and we rate Kredyt Bank Sell.

Valuation

Our Standard Warranted Equity Valuation of ZI 12.0 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. We assume sustainable return on equity of 12.5% and use a cost of equity of 11.5% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 12.1 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). In line with the approach we adopt for the rest of our coverage universe, our target price is based upon the shorter-term approach at ZI 12.0.

Risks

We rate Bank Kredyt Bank Medium Risk based on our assessment of industry- and company-specific risk factors. Risks relating to the Polish banking market include: (1) the Polish banking market is rather fragmented and increased competition could put more pressure on margins and earnings than we currently expect. (2) The macro economy may perform better or worse than anticipated and lead to higher or lower provisioning and slower or faster loan growth than anticipated. Specific to the bank we outline that: (1) historically profitability was lower than its peer group; (2) due to its lower market [share, there is a risk that Kredyt Bank will be more affected by rising competition than peers; (3) the bank is heavily dependent on KBC support; and (4) the sale of Kredyt Bank by KBC, if done via public tender for 100% of the shares at the 6-month average, would imply material upside for minorities. These factors could cause the stock price to outperform, or fall below, our price target.

BGZ

Company description

Bank BGZ is a medium-sized Polish universal bank, specialising in Food and Agriculture (about 2/5 of loans are granted to farmers and food producers, 2/5 to retail clients and 1/5 to other corporate clients). The bank focuses on growth in smaller towns and intends to be "the local bank", combining the comprehensive product offer of a commercial bank with close client relationships, characteristic of cooperative banks.

The bank is controlled by the Dutch cooperative bank Rabobank (59.35% shareholder), while the Polish State Treasury holds 25.2% of the bank's shares.

Investment strategy

Currently, BGZ is Poland's 11th-largest commercial bank in terms of assets and loans, 10th-largest in terms of deposits, 12th-largest in terms of equity and 8th-largest in terms of number of branches. Due to its strong presence in less penetrated smaller towns, planned investments and continued growth in its core F&A division, we expect the bank to increase in scale over the medium term, which should allow it to improve its currently high cost-to-income ratio (75% in 2010) and low ROE (5%). We expect this to drive a convergence of the bank's ROE closer to the sector average by 2015, when we forecast the bank will generate an ROE of 11%. We rate the BGZ Buy.

Valuation

Our Standard Warranted Equity Valuation of ZI 60.3 per share is based upon the formula: $\text{Price} / \text{Book value} = (\text{Sustainable RoE} - \text{growth}) / (\text{Cost of equity} - \text{growth})$. We assume a sustainable ROE of 11% and use a cost of equity of 10.5% and a sustainable growth rate of 5.0%. Our Economic Value Added Valuation of ZI 58.7 per share is equal to the sum of the net present value of the bank's future economic value-added (earnings adjusted for excess equity, less a capital charge reflecting the opportunity cost of capital). As is the case with other Polish banks, we set our target price using the more short-term approach at ZI 60.3.

Risks

We rate BGZ Low Risk after assessing industry- and company-specific risks that may affect the stock achieving our target price. Risks to the Polish banking market include: (1) the possibility of adverse movements in interest rates and bond yields, which could affect earnings; and (2) the macro economy may perform better or worse than anticipated and lead to higher or lower provisioning and slower or faster loan growth than anticipated; (3) In recent years, the number of banks in Poland hasn't materially decreased as recent mergers between some third-tier banks have been largely offset by the launch of start-ups. Simultaneously, starting from 2010, many banks that previously focused on selected parts of the market (mainly on consumer finance) introduced new strategies to become universal banks, leading to competition risk; (4) There is a risk that, in the future, the regulator will try to reduce the banks' appetite for risk, which may make it more difficult for BGZ to implement its strategy; (5) The Polish Ministry of Finance is working on legislation that would introduce a bank levy. However, the detailed structure of the tax and its impact on the profitability of banks are unknown. Specifically, for BGZ, we highlight: (1) the bank's large exposure to the two closely related industries: farmers and food producers; (2) risk related to the planned launch of the direct bank in 2Q11; (3) due to low profitability, earnings are more than averagely sensitive to revenue trends; (3) we note strategic shareholder risk as Rabobank, BGZ's majority shareholder (holding 59%), is a conservatively run bank and is managed based on a very long-term perspective. While we appreciate this strategy, we note that equity investors tend to focus on short-term performance and that differences in investment strategies may lead to some conflict between Rabobank and minority shareholders

Notes

Appendix A-1

Analyst Certification

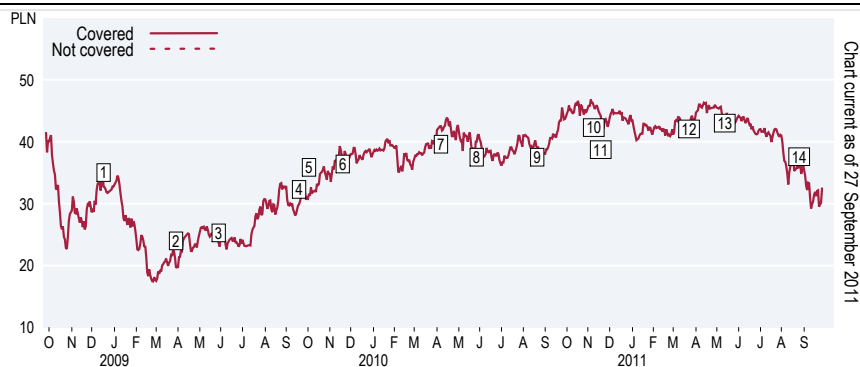
The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

PKO BP (PKOB.WA)

Ratings and Target Price History Fundamental Research

Analyst: Andrzej Powierza
Covered since March 2 2011



	Date	Rating	Target Price	Closing Price
1	17-Dec-08	*2M	*36.91	32.76
2	30-Mar-09	*1M	*27.22	19.64
3	28-May-09	*2M	*28.60	23.62
4	18-Sep-09	*1M	*35.16	29.90
5	2-Oct-09	*2M	*33.90	31.59

* Indicates change

	Date	Rating	Target Price	Closing Price
6	19-Nov-09	*1M	*46.00	36.40
7	7-Apr-10	*1L	*48.40	42.50
8	27-May-10	1L	*49.00	40.00
9	20-Aug-10	1L	*54.00	38.98
10	9-Nov-10	1L	*55.00	45.76

	Date	Rating	Target Price	Closing Price
11	18-Nov-10	1L	*60.00	44.19
12	23-Mar-11	1L	*55.50	42.40
13	12-May-11	*2L	*47.70	43.35
14	25-Aug-11	*1L	*42.90	35.90

Rating/target price changes above reflect Eastern Standard Time

PKO BP (PKOB.WA)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Andrzej Powierza
Covered since March 2 2011



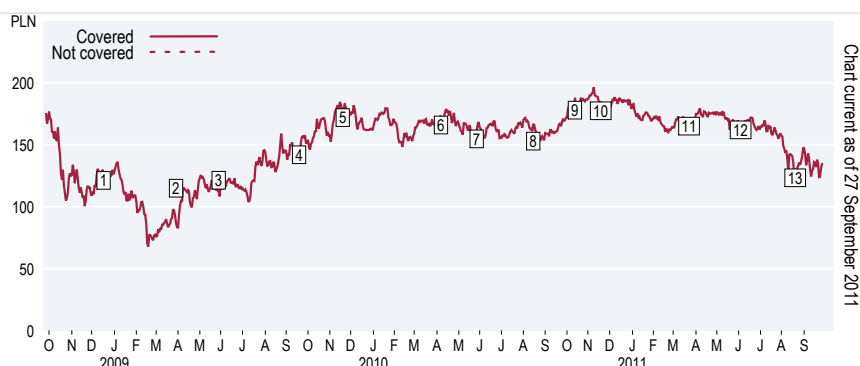
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Bank Pekao SA (BAPE.WA)

Ratings and Target Price History Fundamental Research

Analyst: Andrzej Powierza
Covered since March 2 2011



	Date	Rating	Target Price	Closing Price
1	17-Dec-08	2L	*127.00	121.30
2	30-Mar-09	*1L	*111.90	86.60
3	28-May-09	*3L	*111.10	111.70
4	18-Sep-09	*2L	*151.50	144.40
5	19-Nov-09	2L	*190.00	176.40

* Indicates change

	Date	Rating	Target Price	Closing Price
6	7-Apr-10	2L	*192.00	172.90
7	27-May-10	*1L	*179.50	161.60
8	16-Aug-10	1L	*183.00	166.90
9	13-Oct-10	*2L	183.00	188.00
10	18-Nov-10	2L	*201.00	185.00

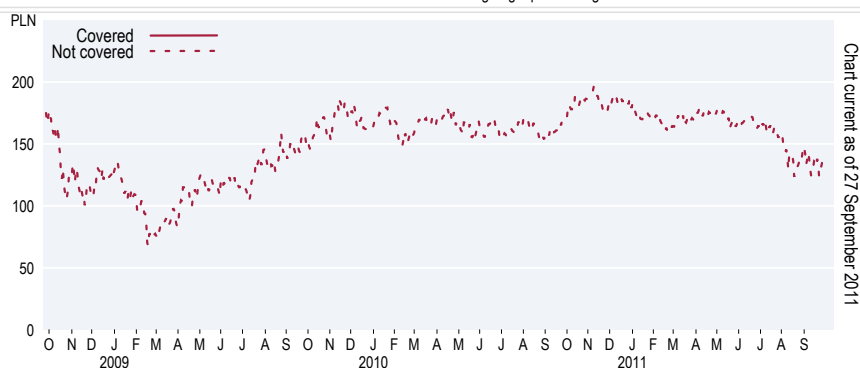
	Date	Rating	Target Price	Closing Price
11	23-Mar-11	*1L	*195.30	166.50
12	3-Jun-11	1L	*186.00	168.00
13	19-Aug-11	1L	*190.00	129.60

Rating/target price changes above reflect Eastern Standard Time

Bank Pekao SA (BAPE.WA)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Andrzej Powierza
Covered since March 2 2011



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

BGZ (BGZ.WA)

Ratings and Target Price History Fundamental Research

Analyst: Andrzej Powierza
Covered since August 2 2011



	Date	Rating	Target Price	Closing Price
1	1-Aug-11	*1L	*66.80	55.80

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

BGZ (BGZ.WA)

Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Andrzej Powierza

Covered since August 2 2011

* Indicates change



Bank Millennium SA (BIGW.WA)

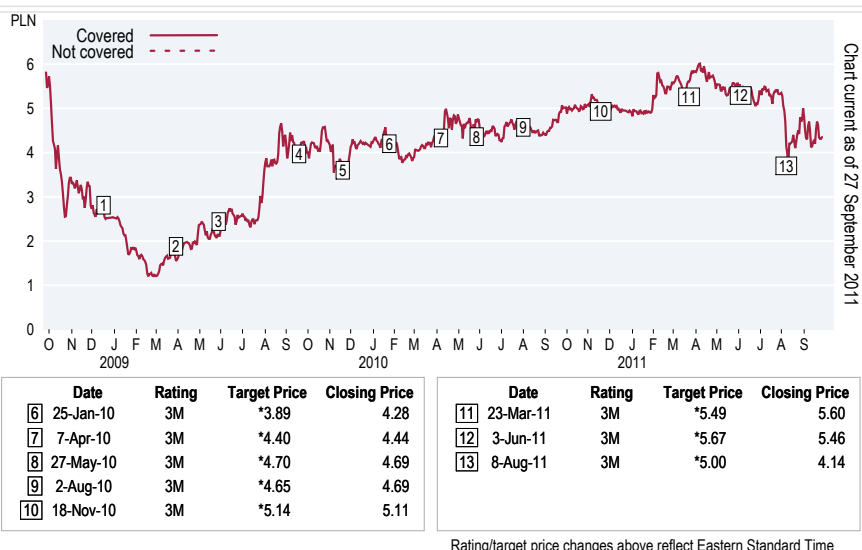
Ratings and Target Price History

Fundamental Research

Analyst: Andrzej Powierza

Covered since March 2 2011

* Indicates change



Date	Rating	Target Price	Closing Price
1 17-Dec-08	*2M	*3.09	2.68
2 30-Mar-09	*3M	*1.67	1.55
3 28-May-09	3M	*1.75	2.12
4 18-Sep-09	3M	*2.43	4.07
5 19-Nov-09	3M	*3.61	3.60

Date	Rating	Target Price	Closing Price
6 25-Jan-10	3M	*3.89	4.28
7 7-Apr-10	3M	*4.40	4.44
8 27-May-10	3M	*4.70	4.69
9 2-Aug-10	3M	*4.65	4.69
10 18-Nov-10	3M	*5.14	5.11

Date	Rating	Target Price	Closing Price
11 23-Mar-11	3M	*5.49	5.60
12 3-Jun-11	3M	*5.67	5.46
13 8-Aug-11	3M	*5.00	4.14

Bank Millennium SA (BIGW.WA)

Ratings and Target Price History

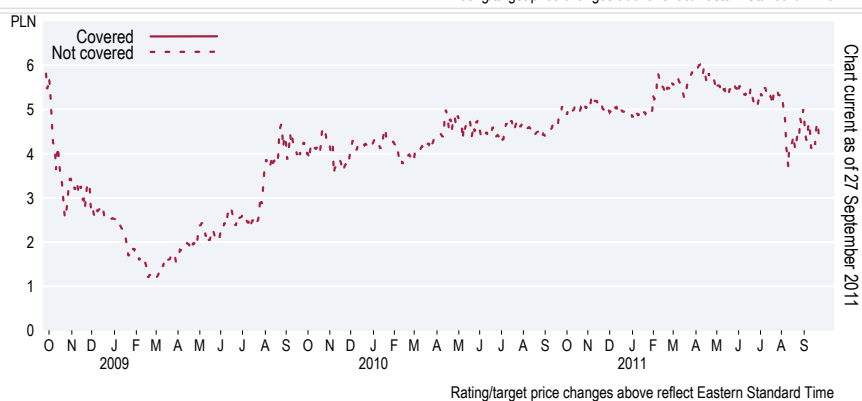
Best Ideas Research

Relative Call (3 Month)

Analyst: Andrzej Powierza

Covered since March 2 2011

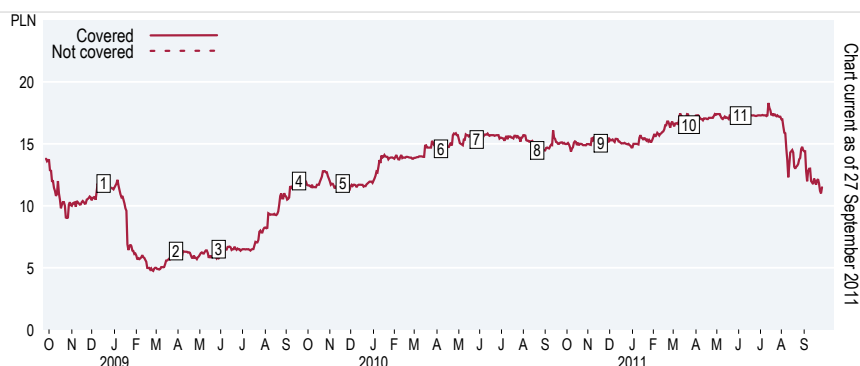
* Indicates change



Kredyt Bank SA (BKRE.WA)

Ratings and Target Price History Fundamental Research

Analyst: Andrzej Powierza
Covered since March 2 2011



	Date	Rating	Target Price	Closing Price
1	17-Dec-08	3M	*9.20	11.51
2	30-Mar-09	3M	*5.70	6.10
3	28-May-09	*2M	*6.46	5.77
4	18-Sep-09	*3M	*9.60	11.70

* Indicates change

	Date	Rating	Target Price	Closing Price
5	19-Nov-09	*2M	*12.80	11.50
6	7-Apr-10	*3M	*15.60	14.80
7	27-May-10	3M	*16.00	15.92
8	20-Aug-10	3M	*15.10	15.00

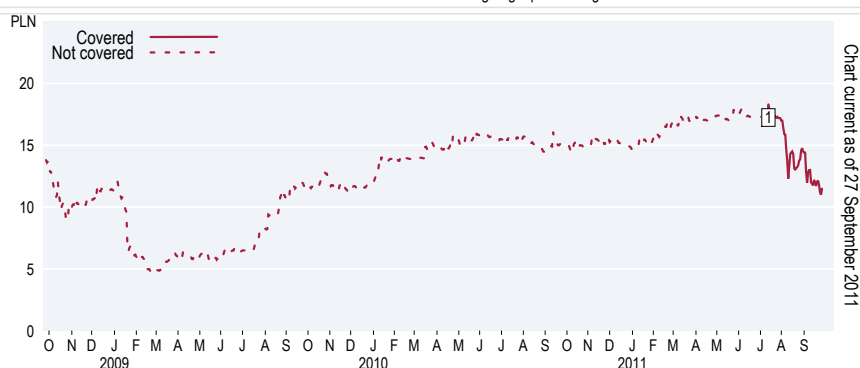
	Date	Rating	Target Price	Closing Price
9	18-Nov-10	3M	*16.00	15.40
10	23-Mar-11	3M	*16.40	17.01
11	3-Jun-11	3M	*16.10	17.78

Rating/target price changes above reflect Eastern Standard Time

Kredyt Bank SA (BKRE.WA)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Andrzej Powierza
Covered since March 2 2011



	Date	Rating	Target Price	Closing Price
1	13-Jul-11	*ADD LP	-	18.30

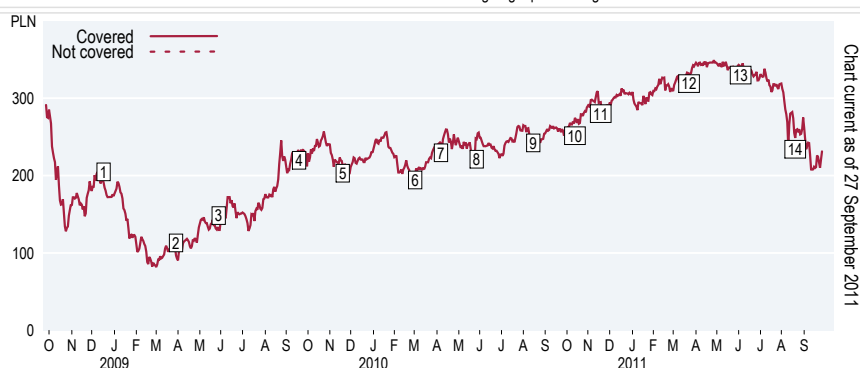
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

BRE Bank SA (BREP.WA)

Ratings and Target Price History Fundamental Research

Analyst: Andrzej Powierza
Covered since March 2 2011



	Date	Rating	Target Price	Closing Price
1	17-Dec-08	*3M	*129.77	191.13
2	30-Mar-09	3M	*84.48	96.84
3	28-May-09	3M	*104.08	129.77
4	18-Sep-09	3M	*169.41	230.76
5	19-Nov-09	3M	*231.29	212.49

* Indicates change

	Date	Rating	Target Price	Closing Price
6	2-Mar-10	*1M	*242.77	201.90
7	7-Apr-10	*2M	*268.37	241.00
8	27-May-10	*1M	*279.00	247.20
9	16-Aug-10	*2M	*273.00	245.00
10	13-Oct-10	*3M	273.00	274.50

	Date	Rating	Target Price	Closing Price
11	18-Nov-10	*2M	*337.00	294.90
12	23-Mar-11	2M	*364.00	328.00
13	3-Jun-11	2M	*351.00	338.90
14	19-Aug-11	2M	*318.00	248.60

Rating/target price changes above reflect Eastern Standard Time

BRE Bank SA (BREP.WA)

Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Andrzej Powierza
Covered since March 2 2011

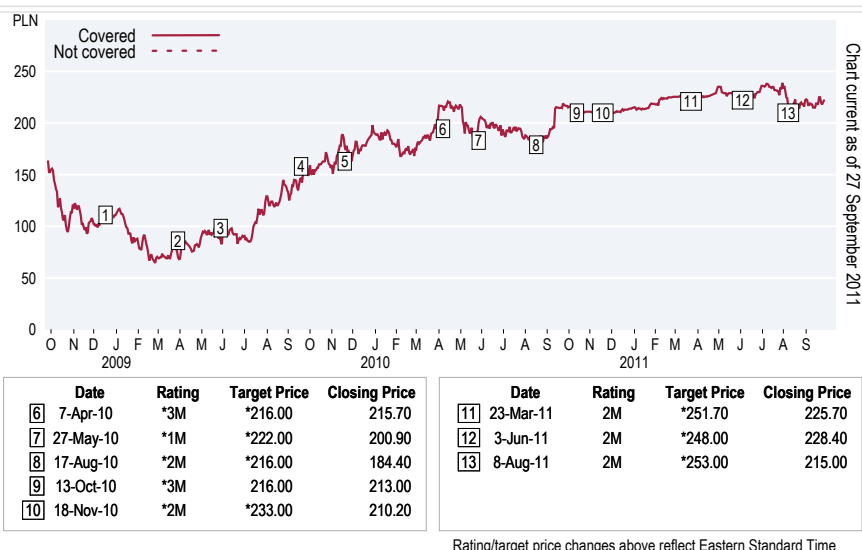


Bank Zachodni WBK (BZWB.WA)

Ratings and Target Price History

Fundamental Research

Analyst: Andrzej Powierza
Covered since March 2 2011



Date	Rating	Target Price	Closing Price
1 17-Dec-08	2M	*120.00	109.00
2 30-Mar-09	2M	*90.60	69.90
3 28-May-09	2M	*98.70	86.10
4 18-Sep-09	*3M	*135.60	146.50
5 19-Nov-09	*2M	*206.00	177.00

Date	Rating	Target Price	Closing Price
6 7-Apr-10	*3M	*216.00	215.70
7 27-May-10	*1M	*222.00	200.90
8 17-Aug-10	*2M	*216.00	184.40
9 13-Oct-10	*3M	216.00	213.00
10 18-Nov-10	*2M	*233.00	210.20

Date	Rating	Target Price	Closing Price
11 23-Mar-11	2M	*251.70	225.70
12 3-Jun-11	2M	*248.00	228.40
13 8-Aug-11	2M	*253.00	215.00

Bank Zachodni WBK (BZWB.WA)

Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Andrzej Powierza
Covered since March 2 2011



ING Bank Slaski SA (SLAS.WA)

Ratings and Target Price History Fundamental Research

Analyst: Andrzej Powierza
Covered since March 2 2011

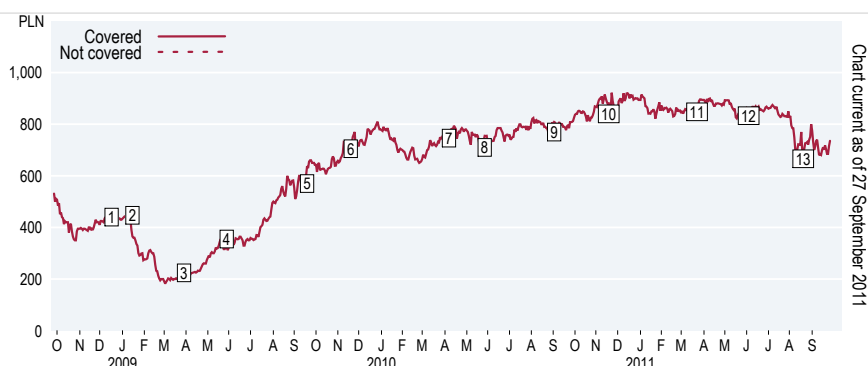


Chart current as of 27 September 2011

	Date	Rating	Target Price	Closing Price
1	17-Dec-08	*2M	*464.00	430.00
2	15-Jan-09	2M	*433.00	365.00
3	30-Mar-09	*1M	*275.00	204.80
4	28-May-09	*3M	*338.00	326.70
5	18-Sep-09	3M	*505.00	637.50

* Indicates change

	Date	Rating	Target Price	Closing Price
6	19-Nov-09	3M	*747.00	715.00
7	7-Apr-10	3M	*777.00	766.00
8	27-May-10	*2M	*809.00	755.00
9	2-Sep-10	*3M	*823.00	808.50
10	18-Nov-10	3M	*920.00	880.00

	Date	Rating	Target Price	Closing Price
11	23-Mar-11	3M	*895.00	877.00
12	3-Jun-11	3M	*899.00	855.00
13	19-Aug-11	*1M	*930.00	690.50

Rating/target price changes above reflect Eastern Standard Time

ING Bank Slaski SA (SLAS.WA)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Andrzej Powierza
Covered since March 2 2011

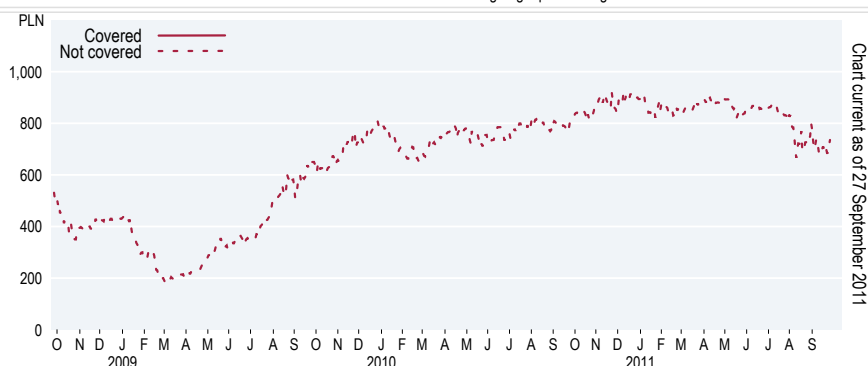


Chart current as of 27 September 2011

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

DMBH is a market maker in the publicly traded equity securities of PKO BP. DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy (1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients.

DMBH is a market maker in the publicly traded equity securities of Bank Pekao SA. DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy (1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients.

DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy (1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients.

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DMBH has received compensation from Bank Zachodni WBK for providing market maker services in the past 12 months. DMBH is a market maker in the publicly traded equity securities of Bank Zachodni WBK. DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy (1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients.

DMBH has received compensation from GPW for providing market maker services in the past 12 months. DMBH is a market maker in the publicly traded equity securities of GPW. DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy

(1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients.

DMBH is a market maker in the publicly traded equity securities of PZU. DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy (1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients. Michal Fidelus, Assistant, holds a long position in the shares of Powszechny Zaklad Ubezpieczen SA.

DMBH rating distribution versus Investment Banking service provision in the past 12 months as at 30 June 2011 is as follows: Buy (1) representing 30% of the DMBH coverage 0% of which are IB clients, Hold (2) representing 36% of the DMBH coverage 0% of which are IB clients, Sell (3) representing 34% of the DMBH coverage 0% of which are IB clients.

A member of the household of Andrzej Powierza, Analyst, holds a long position in the securities of PKO BP.

Within the past 12 months, Citigroup Global Markets Inc. or its affiliates has acted as manager or co-manager of an offering of securities of Bank Pekao SA, BGZ, BRE Bank SA, GPW, ING Bank Slaski SA.

Citigroup Global Markets Inc. or its affiliates has received compensation for investment banking services provided within the past 12 months from PKO BP, Bank Pekao SA, BGZ, Bank Millennium SA, Kredyt Bank SA, BRE Bank SA, Bank Zachodni WBK, GPW, PZU, ING Bank Slaski SA.

Citigroup Global Markets Inc. or its affiliates expects to receive or intends to seek, within the next three months, compensation for investment banking services from PKO BP, BRE Bank SA, Bank Zachodni WBK, GPW, PZU, ING Bank Slaski SA.

Citigroup Global Markets Inc. or an affiliate received compensation for products and services other than investment banking services from PKO BP, Bank Pekao SA, BGZ, Bank Millennium SA, Kredyt Bank SA, BRE Bank SA, Bank Zachodni WBK, GPW, PZU, ING Bank Slaski SA in the past 12 months.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as investment banking client(s): PKO BP, Bank Pekao SA, BGZ, Bank Millennium SA, Kredyt Bank SA, BRE Bank SA, Bank Zachodni WBK, GPW, PZU, ING Bank Slaski SA.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as clients, and the services provided were non-investment-banking, securities-related: PKO BP, Bank Pekao SA, BGZ, Bank Millennium SA, Kredyt Bank SA, BRE Bank SA, Bank Zachodni WBK, GPW, PZU, ING Bank Slaski SA.

Citigroup Global Markets Inc. currently has, or had within the past 12 months, the following as clients, and the services provided were non-investment-banking, non-securities-related: PKO BP, Bank Pekao SA, BGZ, Bank Millennium SA, Kredyt Bank SA, BRE Bank SA, Bank Zachodni WBK, GPW, PZU, ING Bank Slaski SA.

Analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Citigroup Global Markets Inc. and its affiliates ("the Firm"). Like all Firm employees, analysts receive compensation that is impacted by overall firm profitability which includes investment banking revenues.

For important disclosures (including copies of historical disclosures) regarding the companies that are the subject of this Citi Investment Research & Analysis product ("the Product"), please contact Citi Investment Research & Analysis, 388 Greenwich Street, 28th Floor, New York, NY, 10013, Attention: Legal/Compliance [E6WYB6412478]. In addition, the same important disclosures, with the exception of the Valuation and Risk assessments and historical disclosures, are contained on the Firm's disclosure website at www.citigroupgeo.com. Valuation and Risk assessments can be found in the text of the most recent research note/report regarding the subject company. Historical disclosures (for up to the past three years) will be provided upon request.

Citi Investment Research & Analysis Ratings Distribution

Data current as of 30 Jun 2011	12 Month Rating			Relative Rating		
	Buy	Hold	Sell	Buy	Hold	Sell
Citi Investment Research & Analysis Global Fundamental Coverage	54%	36%	11%	10%	81%	10%
% of companies in each rating category that are investment banking clients	45%	41%	42%	50%	42%	44%

Guide to Citi Investment Research & Analysis (CIRA) Fundamental Research Investment Ratings:

CIRA's stock recommendations include a risk rating and an investment rating.

Risk ratings, which take into account both price volatility and fundamental criteria, are: Low (L), Medium (M), High (H), and Speculative (S).

Investment ratings are a function of CIRA's expectation of total return (forecast price appreciation and dividend yield within the next 12 months) and risk rating.

Analysts may place covered stocks "Under Review" in response to exceptional circumstances (e.g. lack of information critical to the analyst's thesis) affecting the company and/or trading in the company's securities (e.g. trading suspension). Stocks placed "Under Review" will be monitored daily by management. As soon as practically possible, the analyst will publish a note re-establishing a rating and investment thesis.

To satisfy regulatory requirements, we correspond Under Review to Hold in our ratings distribution table for our 12-month fundamental rating system. However, we reiterate that we do not consider Under Review to be a recommendation.

Relative three-month ratings: CIRA may also assign a three-month relative call (or rating) to a stock to highlight expected out-performance (most preferred) or under-performance (least preferred) versus the geographic and industry sector over a 3 month period. The relative call may highlight a specific near-term catalyst or event impacting the company or the market that is anticipated to have a short-term price impact on the equity securities of the company. Absent any specific catalyst the analyst(s) will indicate the most and least preferred stocks in the universe of stocks under consideration, explaining the basis for this short-term view. This three-month view may be different from and does not affect a stock's fundamental equity rating, which reflects a longer-term total absolute return expectation. For purposes of NASD/NYSE ratings-distribution-disclosure rules, most preferred calls correspond to a buy recommendation and least preferred calls correspond to a sell recommendation. Any stock not assigned to a most preferred or least preferred call is considered non-relative-rated (NRR). For purposes of NASD/NYSE ratings-distribution-disclosure rules we correspond NRR to Hold in our ratings distribution table for our 3-month relative rating system. However, we reiterate that we do not consider NRR to be a recommendation.

For securities in emerging markets (Asia Pacific, Emerging Europe/Middle East/Africa, and Latin America), investment ratings are: Buy (1) (expected total return of 15% or more for Low-Risk stocks, 20% or more for Medium-Risk stocks, 30% or more for High-Risk stocks, and 40% or more for Speculative stocks); Hold (2) (5%-15% for Low-Risk stocks, 10%-20% for Medium-Risk stocks, 15%-30% for High-Risk stocks, and 20%-40% for Speculative stocks); and Sell (3) (5% or less for Low-Risk stocks, 10% or less for Medium-Risk stocks, 15% or less for High-Risk stocks, and 20% or less for Speculative stocks).

Investment ratings are determined by the ranges described above at the time of initiation of coverage, a change in investment and/or risk rating, or a change in target price (subject to limited management discretion). At other times, the expected total returns may fall outside of these ranges because of market price movements and/or other short-term volatility or trading patterns. Such interim deviations from specified ranges will be permitted but will become subject to review by Research Management. Your decision to buy or sell a security should be based upon your personal investment objectives and should be made only after evaluating the stock's expected performance and risk.

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Non-US research analysts who have prepared this report (i.e., all research analysts listed below other than those identified as employed by Citigroup Global Markets Inc.) are not registered/qualified as research analysts with FINRA. Such research analysts may not be associated persons of the member organization and therefore may not be subject to the NYSE Rule 472 and NASD Rule 2711 restrictions on communications with a subject company, public appearances and trading securities held by a research analyst account. The legal entities employing the authors of this report are listed below:

Dom Maklerski Banku Handlowego SA

Andrzej Powierza

Citigroup Global Markets Ltd

Simon Nellis

OTHER DISCLOSURES

The subject company's share price set out on the front page of this Product is quoted as at 28 September 2011 04:30 PM on the issuer's primary market.

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