

Julius Baer Gruppe AG (BAER.VX)

Dissecting the Bull & Bear Case – Downgrading to Neutral

- **Taking on a Challenge** – Baer has announced the acquisition of Merrill Lynch's International Wealth Management (IWM) business in a complex transaction that will see AuM transferred to Baer at a price/AuM of 1.2%. Whilst cheap versus historic transactions, Baer faces a significant challenge in integrating a business of the size and scope of IWM on to its own platform whilst retaining the most profitable relationship managers in competitive growth markets (see [Asian Private Banking - Key Themes From Hong Kong Meetings](#) (25 June 2012) for the near term challenges in Asia).
- **Acquisition is Underwhelming** – Baer disclosed few financials for IWM, but the lowering of its group targets hints at the profitability of the business. Based on our forecasts for IWM, which appear closer to Baer's bull case for IWM, the acquisition looks underwhelming, with a return on invested capital of 11%. For a more impressive ROIC, we think Baer will have to deliver a better revenue margin and/or cost-income ratio than we see as plausible (see Figure 3). Furthermore, we estimate a share buyback with excess capital would have been at least as accretive as the acquisition and capital raise Baer has opted to pursue.
- **Capital Coffers Look Depleted** – Pro-forma for the acquisition of SFr65bn of IWM AuM (the mid-point of Baer's indicative range) and expected capital effects (e.g. Basel 3, a US-Swiss settlement fine), we view Baer's excess capital position as essentially depleted (see Figure 5). Furthermore, restructuring costs and organic growth should significantly reduce capital generation in 2013E as well.
- **Baer Has it All to Prove, Downgrading to Neutral** – With the stock down 11% following the announcement of the acquisition, management will likely use the upcoming rights issue to convince investors of the merits of the acquisition, possibly with more transparency on financial forecasts. However, integrating the rights issue and acquisition into our forecasts lowers our 2013E-2014E estimates by 7-11% and removes excess capital from our valuation - we lower our target price to SFr33.3 (from SFr41.5) and lower our recommendation on the stock from Buy to Neutral on valuation grounds.

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

Neutral	2
<i>from Buy</i>	
Price (16 Aug 12)	SFr31.88
Target price	SFr33.30
<i>from SFr41.50</i>	
Expected share price return	4.5%
Expected dividend yield	1.9%
Expected total return	6.3%
Market Cap	SFr6,261M
	US\$6,405M

Price Performance (RIC: BAER.VX, BB: BAER VX)



Julius Baer Gruppe AG (CHF)

Year to 31 Dec	2010A	2011A	2012E	2013E	2014E
Net Income (SFrM)	502.0	450.8	446.4	514.7	648.7
Diluted EPS (SFr)	2.43	2.23	2.21	2.33	2.88
Diluted EPS (Old) (SFr)	2.43	2.23	2.23	2.61	3.11
PE (x)	13.1	14.3	14.4	13.7	11.1
P/BV (x)	1.5	1.5	1.4	1.4	1.4
DPS (SFr)	0.60	1.00	0.60	0.60	0.60
Net Div Yield (%)	1.9	3.1	1.9	1.9	1.9
ROE (%)	8.1	5.8	7.8	2.7	8.4

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Fiscal year end 31-Dec	2010	2011	2012E	2013E	2014E
Valuation Ratios					
P/E adjusted (x)	13.1	14.3	14.4	13.7	11.1
P/E reported (x)	18.7	25.1	18.1	51.2	16.8
P/BV (x)	1.5	1.5	1.4	1.4	1.4
P/Adjusted BV diluted (x)	1.5	1.5	1.4	1.4	1.4
Dividend yield (%)	1.9	3.1	1.9	1.9	1.9
Per Share Data (\$Fr)					
EPS adjusted	2.43	2.23	2.21	2.33	2.88
EPS reported	1.70	1.27	1.76	0.62	1.90
BVPS	21.75	21.79	23.49	22.35	22.82
Tangible BVPS	13.02	13.16	15.84	11.40	11.99
Adjusted BVPS diluted	21.75	21.79	23.49	22.35	22.82
DPS	0.60	1.00	0.60	0.60	0.60
Profit & Loss (\$Frm)					
Net interest income	455	532	567	680	821
Fees and commissions	980	942	1,003	1,207	1,427
Other operating Income	358	278	220	266	319
Total operating income	1,794	1,753	1,790	2,153	2,566
Total operating expenses	-1,168	-1,190	-1,239	-1,508	-1,761
Oper. profit bef. provisions	626	563	551	645	806
Bad debt provisions	-25	-24	-20	-29	-34
Non-operating/exceptionals	-168	-220	-91	-377	-221
Pre-tax profit	433	319	440	239	551
Tax	-82	-62	-85	-101	-123
Extraord./Min. Int./Pref. Div.	0	0	0	0	0
Attributable profit	351	257	356	138	428
Adjusted earnings	502	451	446	515	649
Growth Rates (%)					
EPS adjusted	6.3	-8.5	-0.5	5.1	23.8
Oper. profit bef. prov.	6.9	-10.0	-2.1	17.1	24.9
Balance Sheet (\$Frm)					
Total assets	46,287	52,929	56,371	60,881	65,751
Avg interest earning assets	40,567	47,333	57,369	69,819	82,939
Customer loans	14,570	16,408	20,538	24,633	29,026
Gross NPLs	26	18	13	10	8
Liab. & shar. funds	46,287	52,929	56,371	60,881	65,751
Total customer deposits	28,847	34,841	42,951	51,516	60,703
Reserve for loan losses	32	27	23	20	17
Shareholders' equity	4,482	4,308	5,132	5,004	5,164
Profitability/Solvency Ratios (%)					
ROE adjusted	11.6	10.3	9.8	10.2	12.8
Net interest margin	1.12	1.12	0.99	0.97	0.99
Cost/income ratio	65.1	67.9	69.2	70.0	68.6
Cash cost/average assets	na	na	na	na	na
NPLs/customer loans	0.2	0.1	0.1	0.0	0.0
Reserve for loan losses/NPLs	123.6	150.1	182.3	193.7	205.8
Bad debt prov./avg. cust. loans	0.2	0.2	0.1	0.1	0.1
Loans/deposit ratio	50.5	47.1	47.8	47.8	47.8
Tier 1 capital ratio	23.8	21.2	27.3	16.8	16.1
Total capital ratio	23.8	23.3	29.5	19.3	18.3

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Dissecting the Bull & Bear Case

How Profitable is IWM?

BoA/ML's International Wealth Management (IWM) business was broadly breakeven in 2011, with an underlying cost/income ratio of 100% (excluding corporate overheads). Not all of this business is to be acquired – of the SFr81bn of AuM at IWM, Baer has guided that it will take SFr57-72bn - but the downward revision of Baer's medium targets hints that IWM's profitability is expected to be worse than that for standalone Baer.

We use the change in targets to estimate the implied profitability of IWM in Figure 1. Based on our calculations, Baer's targets appear to imply a revenue margin of 70-96bps.

Baer has stated that it sees 70% as the 'go-to' cost-income ratio for IWM – we estimate 80% as an appropriate bear case, based on previous comments by management regarding their Asian operations (see [Swiss Banks - Feedback from Zurich Meetings](#), 28 May 2012).

Figure 1. Julius Baer – Financials Implied by Targets (Citi Calculations)

	Old Targets		New Targets				Citi		
	Bull Case	Bear Case	Bull Case		Bear Case				
	Baer Standalone 2015E	Baer Standalone 2015E	Baer + IWM 2015E	Implied IWM Standalone 2015E	Baer + IWM 2015E	Implied IWM Standalone 2015E	Baer Standalone 2015E	IWM Standalone 2015E	Baer + IWM 2015E
Baer AuM (SFr bn)	250	227	250		227		238		238
IWM AuM (SFr bn)			86		65			75	75
Total Average AuM (SFr bn)	238	219	320	82	282	63	228	73	297
Pre-tax Profit / AuM	0.38%*	0.35%	0.35%	0.28%	0.30%	0.13%	0.34%	0.26%	0.32%
Revenue (SFr m)				791		442	2,287	653	2,931
Costs (SFr m)				(563)		(363)	(1,480)	(457)	(1,937)
Est. Provisions (Citi, SFr m)				(9)		(9)	(28)	(9)	(37)
Pre-tax Profit (SFr m)	893	767	1,122	228	846	79	779	187	957
Operating Metrics									
Revenue Margin %				0.96%		0.70%	1.00%	0.90%	0.98%
Cost/Income %				70%		80%*	65%	70%	66%
Return on Invested Capital				14.2%		6.3%		11.3%	

Source: Company Reports and Citi Research Estimates

Notes:

*Citi estimate

Old targets: Pre-tax Profit / AuM: >35bps; Cost/Income: 62-66%; NNM %: 4-6%

New targets: Pre-tax Profit / AuM: 30-35bps; Cost/Income: 65-70%; NNM %: 4-6%

Bull Case AuM based on 6% NNM growth and 4% market effect; Bear Case AuM based on 4% NNM growth and 3% market effect

Citi estimates of Baer Standalone based on rolled out old Citi estimates with no RM hiring over 2012-2014

Citi Base Case for IWM

Baer disclosed scant details on the profitability of IWM. We form our own view on the profitability of IWM based around the key metrics of revenue margin, cost-income ratio and AuM:

- **Revenue Margin of 90bps** – Baer indicated that its targets assumed IWM started on a revenue margin that was lower than what it currently was, and built up to the level it was seeking to achieve for the standalone Baer business by 2015. In our view, such a build up assumes a sharper recovery in client risk appetite than we currently expect – we take 90bps as our base case.
- **Cost-Income Ratio of 70%** – IWM was break-even in 2011, whilst efficiency gains from Baer management are expected to bring this close to Baer's standalone ratio by 2015. The 30% synergies this implies is broadly inline with the 29% achieved with the acquisition of ING Switzerland (see Baer-ING Up, 2 November 2009). Furthermore, actual synergies required may be less than 30%, as the cost-income ratio for the AuM Baer finally acquires is likely to be less than the 100% for the legacy IWM business.
- **AuM Acquired of SFr65bn** – Baer expects to ultimately purchase SFr57-72bn of AuM. One-third of AuM is to come from the acquisition of legal entities (from which clients may “opt out”), whilst the remaining two thirds is to come from relationship managers joining Baer's platform. We take the mid-point of Baer's indicative range as our base case.
- **Net New Money Growth of 4%** – IWM relationship managers are currently not incentivised to attract new client assets, whilst uncertainty over the new business led to NNM growth of just 1% in 2011. Baer intends to replace IWM's current compensation scheme with one that does explicitly reward NNM. This and the growth markets bias of IWM's operations gives us confidence in assuming NNM of 4%.

We present our forecast financials for IWM in Figure 2.

Figure 2. BoA/ML IWM – Financial Estimates

SFr m	Principal Closing	2013E	% chg	2014E	% chg	2015E	% chg
Revenues		252		490	+94%	653	+33%
Operating Expenses		-214		-380	+77%	-457	+20%
Pre-Provision Profit		38		110	+192%	196	+77%
Provisions		-3.9		-7.1	nm	-8.9	nm
PBT		34		103	+204%	187	+81%
Net Profit		29		87	+204%	157	+81%
AuM (SFr bn)							
AuM Purchased	17	24	+41%	24	+0%	0	-100%
AuM NNM + Market Effect		1.4		3.4	+149%	5.6	+65%
AuM - End of Period	17	42.4	+149%	69.7	+65%	75.3	+8%
Average AuM		29.7		56.1	+89%	72.5	+29%
NNM %		4.0%		4.0%		4.0%	
Market Effect %		4.0%		4.0%		4.0%	
Revenue Margin		0.85%		0.88%		0.90%	
PBT/AuM		0.11%		0.18%		0.26%	
Cost/Income		85%		78%		70%	

Source: Company Reports and Citi Research Estimates

Acquisition Maths – Underwhelming

Despite our forecasts being based on metrics closer to the top end of Baer's new targets, the acquisition of IWM looks underwhelming.

Our estimates imply a 2015E return on invested capital (ROIC) of c11% – broadly inline with Baer's cost of equity. A sensitivity analysis suggests that, under our estimates, a revenue margin of >110bps and/or cost income ratio better (i.e. lower) than 70% would be required to make the acquisition appealing – both significantly higher than we think possible and Baer's best case targets imply.

Figure 3. Acquisition of IWM – Return on Invested Capital (2015E)

		Revenue Margin				
		0.70%	0.80%	0.90%	1.00%	1.10%
Cost/Income	55%	13%	15%	17%	19%	21%
	60%	12%	13%	15%	17%	19%
	65%	10%	12%	13%	15%	16%
	70%	9%	10%	11%	13%	14%
	75%	7%	8%	9%	10%	12%
	80%	6%	6%	7%	8%	9%
	85%	4%	5%	5%	6%	7%

Source: Citi Research

Baer calculated the EPS accretion of the deal as c15% in 2015, excluding the effect of the SFr250m capital raised to replenish its excess capital. We calculate an equivalent figure of 12%. This is benchmarking against a hypothetical standalone Baer that has ceased hiring new relationship managers and suspended share buybacks, both of which we expect Baer to do following this acquisition.

However, accretion falls to 8% after considering the SFr250m of surplus capital being raised. Furthermore, in our view it's more relevant to benchmark this accretion to the alternative of an acquisition – returning capital to shareholders. This is relevant to capture the opportunity cost of Baer's acquisition of IWM. In Figure 4 we consider two scenarios:

- **SFr530m buyback in 2015** - Baer will use SFr530m of excess capital in financing its acquisition. Our analysis indicates the acquisition and extra capital raise is marginally dilutive for shareholders compared to a SFr530m buyback in 2015
- **SFr750m buyback in 2015** – Baer's now cancelled buyback plan called for a capital return of up to SFr500m over two years. Given Baer's capital generative business model, we would have assumed this buyback plan would have been reloaded in 2015, implying SFr750m returned to shareholders over 2013-2015. Relative to a SFr750m buyback in 2015, we estimate Baer's acquisition and excess capital raise is actually 5% dilutive.

Figure 4. IWS Acquisition Scenarios – 2015 Earnings Accretion/Dilution

<u>IWM Acquisition vs No Action</u>				
	Baer Standalone	IWM	Pro-forma	% Change
Adjusted Net Profit	643	161	804	25%
Sharecount	195		218	12%
EPS	3.29		3.68	12%
<u>w/ SFr250m Extra Capital Raise</u>				
	Baer Standalone	IWM	Pro-forma	
Adjusted Net Profit	643	161	804	25%
Sharecount	195		226	16%
EPS	3.29		3.55	8%
<u>w/ SFr250m Extra Capital Raise vs Baer w/ SFr530m Buyback</u>				
	Baer (w/ Buyback)	IWM	Pro-forma	
Adjusted Net Profit	643	161	804	25%
Sharecount	178		226	27%
EPS	3.60		3.55	-1%
<u>w/ SFr250m Extra Capital Raise vs Baer w/ SFr750m Buyback</u>				
	Baer (w/ Buyback)	IWM	Pro-forma	
Adjusted Net Profit	643	161	804	25%
Sharecount	172		226	32%
EPS	3.74		3.55	-5%

Source: Citi Research

We would note that the above analysis is based on Baer's current share price of SFr32. At lower share prices, the accretion of a buyback looks even more favourable versus the acquisition and capital raise.

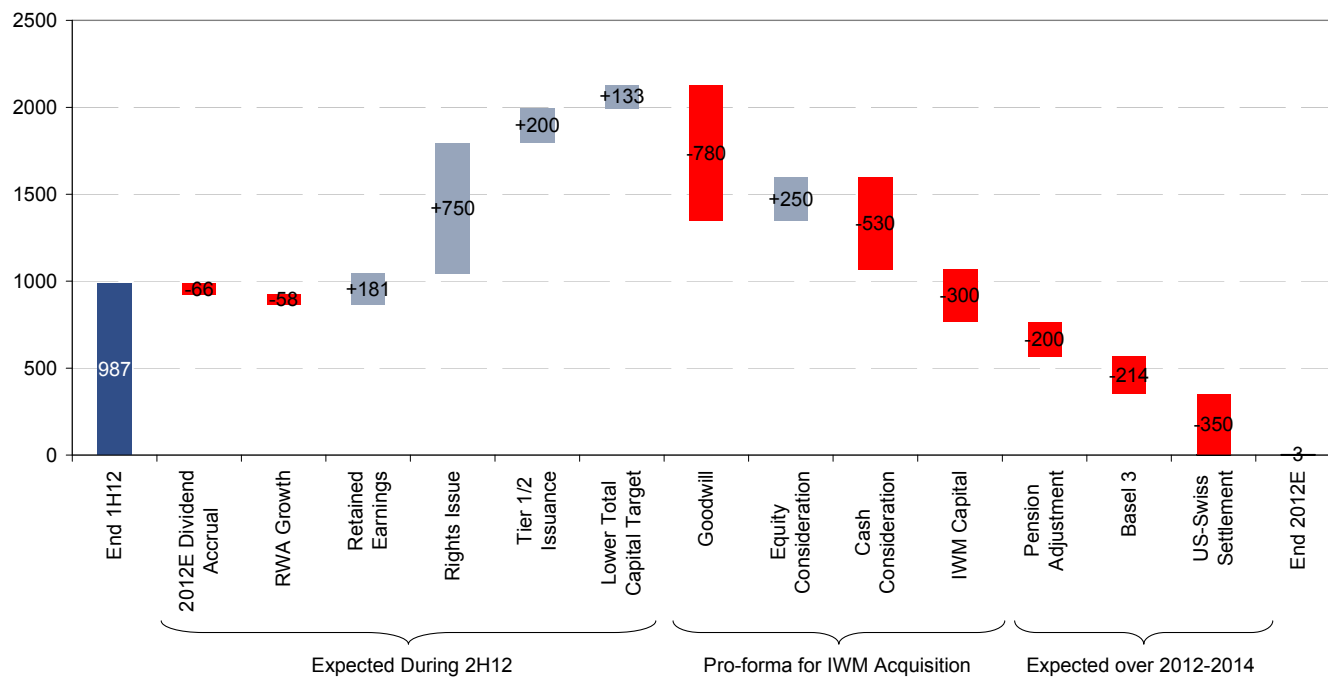
Capital Coffers Look Depleted

At end 1H12, Baer had excess capital of SFr987m (SFr5 per share), whilst lowering its total capital ratio to 15% would have increased this to SFr1.1bn (SFr5.7 per share).

Pro-forma for the acquisition and other known and expected capital deductions, we calculate end-2012 excess capital as essentially zero. However, we would note the following:

- IWM related consideration and capital usage will be deducted from capital over the acquisition timeline (2012-2015)
- The deduction of IWM related goodwill will be on principal closing of the transaction, expected over 4Q12-1Q13
- The pension adjustment and Basel 3 impact are expected as at January 2013, whilst the timing of a US-Swiss settlement fine is currently unknown

Figure 5. Julius Baer – Excess Capital Bridge Pro-forma for Known and Expected Changes, end-2012E

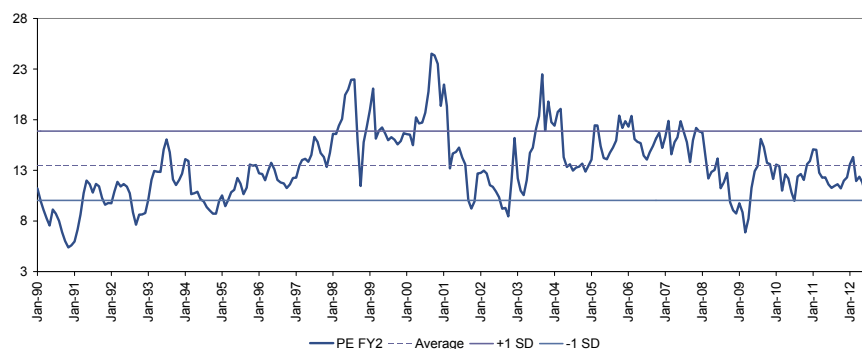


Source: Company Reports and Citi Research Estimates

Valuation

On our revised estimates, Baer trades on a two-year forward PE of 13.8x, broadly inline with its long-term average. Pro-forma for the capital effects of the IWM acquisition (which in reality will be phased over 2-3 years) and for other expected capital effects, we estimate Baer has no excess capital at end-2012E, whilst restructuring charges mean it will likely have none at end-2013E either, hence an excess capital adjustment is unnecessary.

Figure 6. Julius Baer – 2-Year Forward Consensus PE



Source: DataStream

We adjust our PE based valuation approach for our new pro-forma excess capital calculations in Figure 7. Our new estimates imply a target price of SFr33.3 per share.

Figure 7. Julius Baer – Valuation (SFRm)

	2012E	2013E	2014E	Aggregate
Net Income	446	515	649	
Multiple	16.1x	14.0x	12.0x	
Private Banking Value	7,197	7,219	7,800	
NPV of Surplus Capital (total capital above 16%)	0	0	58	
Group Total	7,197	7,219	7,858	
Sharecount	218	224	226	
Fair Value Per Share	32.9	32.2	34.7	33.3
Fair Value Per Share Excluding Surplus Capital	32.9	32.2	34.5	33.2

Source: Citi Research

Estimate Changes

We adjust our estimates for the acquisition of IWM, which is expected to complete over 2012-2014, and Baer's planned SFr750m rights issue. We also remove our previous assumption of SFr250m of shares being bought back per year. Whilst we expect the IWM to make a positive contribution to Julius Baer's financials, change in our share count forecasts drives 2013E-2014E EPS cuts of 7-11%. In light of the size of the IWM acquisition, we assume Baer abandons its previous hiring target of 40-50 advisers per year, which reduces our estimates for organic net new money growth. With this note, we also publish 2015E estimates for the first time.

Figure 8. Julius Baer – Changes to Financial Forecasts, 2012E-2015E

		2012E			2013E			2014E			2015E		
		Old	New	% Chg	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
Total operating income	SFrm	1,752	1,790	+2%	1,931	2,153	+11%	2,133	2,566	+20%	na	2,931	na
Total operating expenses	SFrm	-1,233	-1,259	+2%	-1,333	-1,537	+15%	-1,439	-1,794	+25%	na	-1,974	na
PBT	SFrm	519	531	+2%	598	616	+3%	694	772	+11%	na	957	na
Tax	SFrm	-83	-85	+2%	-98	-101	+3%	-118	-123	+5%	na	-152	na
Net profit - adjusted	SFrm	436	446	+2%	499	515	+3%	576	649	+13%	na	804	na
EPS -- adjusted	SFr	2.23	2.21	-1%	2.61	2.33	-11%	3.11	2.88	-7%	na	3.55	na
Net new money	SFrbn	10.6	9.4	-12%	9.7	8.4	-13%	11.1	9.8	-12%	na	14.0	na
AuM	SFrbn	187.8	203.5	+8%	205.0	244.1	+19%	224.3	287.6	+28%	na	313.1	na
Av AuM	SFrbn	179.9	183.9	+2%	196.4	223.8	+14%	214.6	265.9	+24%	na	300.4	na
BIS Tier 1 Ratio (Basel 2.5)	%	21.6%	27.3%	5.7%	20.7%	16.8%	-3.9%	20.3%	16.1%	-4.3%	na	18.0%	na
Revenue Margin	%	0.97%	0.97%	0.00%	0.98%	0.96%	-0.02%	0.99%	0.97%	-0.03%	na	0.98%	na
Cost/Income Ratio (pro-forma)	%	70%	70%	0%	69%	71%	2%	67%	70%	2%	na	67%	na
Tax Rate (pro-forma)	%	16%	16%	0%	16%	16%	0%	17%	16%	-1%	na	16%	na

Source: Citi Research

Figure 9. Julius Baer – Group Profit and Loss Account by Year

SFr millions	2009	2010	% chg	2011	% chg	2012E	% chg	2013E	% chg	2014E	% chg	2015E	% chg
Group P&L													
Net Interest Income	467	455	-2%	532	+17%	567	+7%	680	+21%	821	+20%	938	+14%
Net Fee and Commission Income	819	980	+20%	942	-4%	1,003	+6%	1,207	+20%	1,427	+18%	1,628	+14%
Net Trading Income	299	332	+11%	269	-19%	192	-29%	233	+21%	279	+20%	318	+14%
Other Ordinary Results	2	26	+996%	9	nm	28	+196%	33	+21%	40	+20%	46	+14%
Revenues	1,586	1,794	+13%	1,753	-2%	1,790	+2%	2,153	+20%	2,566	+19%	2,931	+14%
Personnel Expenses	-683	-791	+16%	-787	-0%	-812	+3%	-995	+23%	-1,162	+17%	-1,278	+10%
General Expenses	-271	-320	+18%	-336	+5%	-363	+8%	-434	+20%	-507	+17%	-559	+10%
Depreciation & Amortisation	-47	-57	+21%	-66	+17%	-65	-2%	-79	+22%	-92	+16%	-100	+9%
Operating Expenses	-1,001	-1,168	+17%	-1,190	+2%	-1,239	+4%	-1,508	+22%	-1,761	+17%	-1,937	+10%
Operating Profit	585	626	+7%	563	-10%	551	-2%	645	+17%	806	+25%	994	+23%
Provisions & valn adjustment	-25	-25		-24		-20		-29	0	-34	0	-37	0
PBT	560	601	+7%	539	-10%	531	-1%	616	+16%	772	+25%	957	+24%
Tax	-87	-99		-88	0%	-85	0%	-101	0%	-123	0%	-152	0%
Net profit	473	502		451	0%	447	0%	515	0%	649	0%	804	0%
Minority interests	0	0		0	0%	0	0%	0	0%	0	0%	0	0%
Attributable profit (adjusted)	473	502	+6%	451	-10%	446	-1%	515	+15%	649	+26%	804	+24%
Restructuring	-12	-66		-130		0		-234		-78		0	
Goodwill/intangibles	-74	-102		-90		-91		-143		-143		-143	
Tax	2	17		26		0		0		0		0	
Attributable profit (reported)	389	351	-10%	257	-27%	356	+38%	138	-61%	428	+210%	661	+55%
PER SHARE FIGURES													
EPS -- as reported	1.88	1.70	-10%	1.27	-25%	1.76	+39%	0.62	-65%	1.90	+205%	2.92	+54%
EPS -- adjusted	2.29	2.43	+6%	2.23	-8%	2.21	-1%	2.33	+5%	2.88	+24%	3.55	+23%
Dividend per share	0.40	0.60		1.00		0.60		0.60	+0%	0.60	+0%	0.60	+0%
Book value per share	20.3	21.7		21.8		23.5		22.3	+0%	22.8	+0%	25.1	+0%
SHARES OUTSTANDING (millions)													
Total dividend-eligible shares (period-end)	206.6	206.1		197.7		218.5		223.9		226.3		226.3	
Total dividend-eligible shares (period-average)	206.7	206.4		202.5		201.6		221.2		225.1		226.3	
OPERATING RATIOS													
Comp ratio (personnel expenses / income)		44.1%		44.9%		45.3%		46.2%		45.3%		43.6%	
Non-comp ratio (other expenses / income)	20.0%	21.0%		23.0%		23.9%		23.8%		23.3%		22.5%	
Cost/Income	63.1%	65.1%		67.9%		69.2%		70.0%		68.6%		66.1%	
Provision charge / avg customer loans	0.24%	0.17%		0.15%		0.10%		0.13%		0.13%		0.12%	
Effective tax rate	16%	16%		16%		16%		16%		16%		16%	
Return on Equity as reported	10%	8%		6%		8%		3%		8%		12%	
Return on Equity (adjusted)	12%	12%		10%		10%		10%		13%		15%	
AUM DATA													
Advisors	667	752	+13%	795	+6%	816	+3%	973	+19%	1129	+16%	1179	+4%
Assets under Management	153,600	169,700	+10%	170,300	+0%	203,508	+19%	244,088	+20%	287,615	+18%	313,124	+9%
AuM (average)	143,200	170,700	+19%	167,550	-2%	183,877	+10%	223,798	+22%	265,852	+19%	300,370	+13%
Net New Money / AuM	4%	6%		6%		6%		4%		4%		5%	
Net New Money	+5,106	+8,800		+10,200		+9,376		+8,440		+9,764		+14,005	
Revenues/Avg AuM	1.11%	1.05%		1.05%		0.97%		0.96%		0.97%		0.98%	
PBT / avg AuM (adjusted)	0.39%	0.35%		0.32%		0.29%		0.28%		0.29%		0.32%	
NII / Avg Footings	1.24%	1.05%		1.04%		0.89%		0.97%		0.99%		1.00%	
BALANCE SHEET ITEMS													
Shareholders equity excl minorities	4,192	4,482	+7%	4,308	-4%	5,132	+19%	5,004	-3%	5,164	+3%	5,690	+10%
Risk-Weighted Assets (Basel 2.5)	10,970	12,061	+10%	12,811	+6%	13,323	+4%	15,566	+17%	17,267	+11%	18,303	+6%
Tier 1 capital (Basel 2.5)	2,656	2,873	+8%	2,710	-6%	3,635	+34%	2,615	-28%	2,773	+6%	3,299	+19%
Tier 1 ratio (Basel 2.5)	24.2%	23.8%		21.2%		27.3%		16.8%		16.1%		18.0%	
Core Tier 1 ratio (Basel 2.5)	22.2%	22.0%		19.4%		25.6%		14.7%		14.2%		16.2%	
Total ratio (Basel 2.5)	24.2%	23.8%		23.3%		29.5%		19.3%		18.3%		20.2%	

Source: Company Reports and Citi Research Estimates

Figure 10. Julius Baer — Group Profit and Loss Account by Half-Year

SFr millions	1H08	2H08	1H09	2H09	1H10	2H10	1H11	2H11	1H12	2H12E
Net Interest Income	213	241	281	186	245	210	316	216	323	245
Net Fee and Commission Income	504	464	393	426	492	488	496	446	471	532
Net Trading Income	172	170	151	147	163	169	86	183	52	140
Other Ordinary Results	5	-106	-12	15	16	10	-1	10	18	10
Revenues	894	768	813	774	917	877	898	855	863	927
Personnel Expenses	-396	-348	-357	-326	-400	-391	-411	-376	-404	-407
General Expenses	-139	-170	-142	-129	-154	-166	-164	-173	-172	-191
Depreciation & Amortisation	-15	-22	-22	-25	-27	-30	-30	-36	-32	-33
Operating Expenses	-550	-540	-521	-480	-581	-587	-605	-585	-608	-632
Operating Profit	344	229	292	294	336	290	293	270	256	296
Provisions & valn adjustment	-8.8	-22.8	-8.7	-16.0	-12.9	-12.0	3.1	-27.3	10.7	-30.7
PBT	336	206	283	278	323	278	296	243	266	265
Tax	-58	-43	-41	-46	-62	-37	-49	-39	-45	-40
Net profit	278	163	242	231	261	241	247	204	221	225
Minority interests	0	0	0	0	0	0	0	0	0	0
Attributable profit (adjusted)	278	163	242	231	261	241	247	204	221	225
Restructuring	-7	-7	-6	-6	-43	-23	-71	-59	0	0
Goodwill/intangibles	-37	-37	-33	-41	-42	-60	-45	-45	-46	-45
Tax	2	2	0	2	9	8	15	11	0	0
Attributable profit (reported)	236	121	203	186	185	166	146	111	176	180
PER SHARE FIGURES										
EPS -- as reported	1.13	0.58	0.98	0.90	0.90	0.80	0.71	0.56	0.89	0.87
EPS -- adjusted	1.33	0.79	1.17	1.12	1.26	1.17	1.21	1.02	1.13	1.09
Dividend per share										
Book value per share		17.0	17.8	20.3	20.9	21.7	21.6	21.8	21.5	23.5
SHARES OUTSTANDING (millions)										
Total dividend-eligible shares (period-end)	205.6	207.0	206.7	206.6	206.6	206.1	203.2	197.7	195.0	218.5
Total dividend-eligible shares (period-average)	208.3	207.3	206.9	206.7	206.6	206.4	204.6	200.4	196.4	206.8
OPERATING RATIOS										
Comp ratio (personnel expenses / income)	44.2%	45.3%	43.9%	42.2%	43.6%	44.6%	45.8%	44.0%	45.2%	43.9%
Non-comp ratio (other expenses / income)	17.2%	24.9%	20.2%	19.9%	19.7%	22.3%	21.6%	24.4%	23.5%	23.0%
Cost/Income	61.5%	70.2%	64.1%	62.1%	63.4%	66.9%	67.4%	68.4%	70.4%	68.1%
Provision charge / avg customer loans		0.23%	0.09%	0.15%	0.10%	0.08%	-0.02%	0.17%	-0.06%	0.16%
Effective tax rate	17%	21%	14%	17%	19%	13%	17%	16%	17%	15%
Return on Equity as reported			11%	9%	9%	8%	7%	5%	8%	8%
Return on Equity (adjusted)			13%	12%	12%	11%	11%	9%	10%	10%
AUM DATA										
Advisors	568	619	636	667	732	752	794	795	801	816
Assets under Management	148,432	127,595	142,400	153,600	166,063	169,700	165,600	170,300	178,800	203,508
AuM (average)	149,400	143,700	136,100	150,400	170,900	169,800	171,200	163,900	176,600	191,154
Net New Money / AuM	11%	12%	7%	1%	4%	7%	6%	6%	6%	4%
Net New Money	+8,396	+8,837	+4,307	+799	+3,293	+5,507	+4,900	+5,300	+5,500	+3,876
Revenues/Avg AuM	1.20%	1.07%	1.19%	1.03%	1.07%	1.03%	1.05%	1.04%	0.98%	0.97%
PBT / avg AuM (adjusted)	0.45%	0.29%	0.42%	0.37%	0.38%	0.33%	0.35%	0.30%	0.30%	0.28%
NII / Avg Footings		0.68%	0.77%	0.50%	0.61%	0.49%	0.71%	0.44%	0.60%	0.45%
BALANCE SHEET ITEMS										
Shareholders equity excl minorities		3,522	3,679	4,192	4,309	4,482	4,396	4,308	4,202	5,132
Risk-Weighted Assets (Basel 2.5)		13,841	11,978	10,970	11,837	12,061	13,327	12,811	12,935	13,323
Tier 1 capital (Basel 2.5)		1,997	1,964	2,656	2,695	2,873	2,896	2,710	2,766	3,635
Tier 1 ratio (Basel 2.5)		14.4%	16.4%	24.2%	22.8%	23.8%	21.7%	21.2%	21.4%	27.3%
Core Tier 1 ratio (Basel 2.5)		12.8%	14.5%	22.2%	20.9%	22.0%	20.0%	19.4%	19.6%	25.6%
Total ratio (Basel 2.5)		14.4%	16.4%	24.2%	23.4%	24.3%	22.0%	23.3%	23.6%	29.5%

Source: Company Reports and Citi Research Estimates

Julius Baer Gruppe AG

Company description

Julius Baer was founded in the late 1800s and has been listed since 1980, previously as part of Julius Baer Holdings and now as Julius Baer Group. Julius Baer is a Swiss-based pure-play private bank exclusively focused on servicing and advising private clients and independent asset managers. The group operates in some 40 locations through 20 countries and has AuM of cSFr180bn.

Investment strategy

We have a Neutral recommendation on Julius Baer Group. Through the separation with GAM Holding, Julius Baer has returned to its core competency of pure private banking. Private banking offers attractive growth prospects through organic expansion (e.g. Asia) and acquisitions. While low investor risk appetite may put near-term pressure on Baer's P&L, in the longer-term we expect these cyclical pressures to reverse, albeit at a slower pace than they have done so in previous cycles. However, we are cautious on Baer's acquisition of BoA/ML's non-US wealth management business. Whilst the business offers sizeable exposure to emerging markets, Baer faces a challenge in integrating it and improving its profitability.

Valuation

Our primary valuation metric for Julius Baer is an adjusted relative P/E analysis, based on Baer's 2012E-14E earnings. This allows us to capture the company's medium- to long-term prospects and Baer's excess capital position (after adjustments for expected and potential capital deductions). This analysis points to a theoretical valuation of SFr33.3 per share, which we set as our target price.

Risks

The key risks to our investment thesis on Julius Baer are: (1) like other asset gatherers, its AuM base (and thus revenues and profits) are sensitive to movements in markets and currencies, (2) the reforms to Swiss tax/secretary arrangements could cause some client attrition for Baer in common with other private banks, (3) litigation related to tax authorities pursuing citizens hiding untaxed assets in offshore accounts, (4) pressure on cost-income ratio from ongoing investment spend, (5) competitive pricing pressures, and (6) overpaying on future acquisitions.

If any of these risk factors has a greater downside impact than we anticipate, the share price will likely have difficulty attaining our target price.

Appendix A-1

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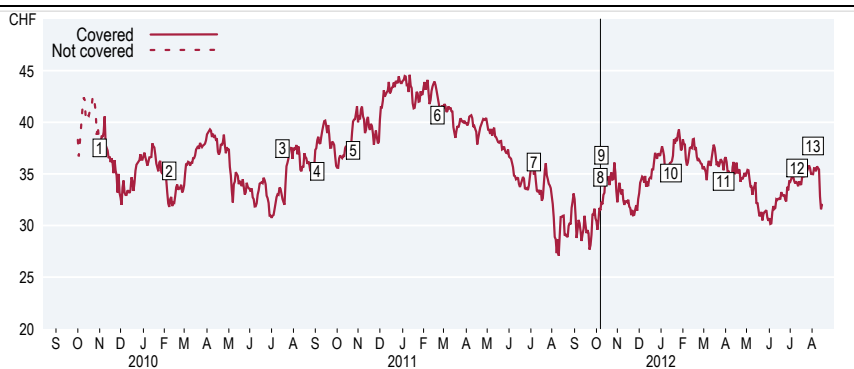
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Julius Baer Gruppe AG (BAER.VX)

Ratings and Target Price History Fundamental Research

Analyst: Sentoor Kanagasabapathy
Covered since November 8 2011



	Date	Rating	Target Price	Closing Price
1	1-Nov-09	*1M	*48.40	38.62
2	7-Feb-10	1M	*45.00	32.13
3	16-Jul-10	1M	*42.00	32.56
4	3-Sep-10	1M	*44.00	38.26
5	25-Oct-10	1M	*48.50	40.07

* Indicates change

	Date	Rating	Target Price	Closing Price
6	21-Feb-11	1M	*53.50	42.54
7	6-Jul-11	1M	*47.00	34.94
8	7-Oct-11	Stock rating system changed		
9	8-Oct-11	*1	47.00	31.47
10	16-Jan-12	1	*45.00	36.10

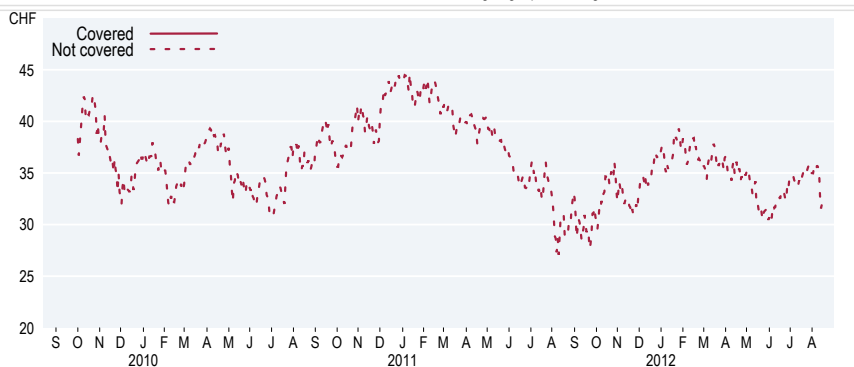
	Date	Rating	Target Price	Closing Price
11	29-Mar-12	1	*45.50	35.35
12	11-Jul-12	1	*42.50	34.10
13	2-Aug-12	1	*41.50	34.97

Rating/target price changes above reflect Eastern Standard Time

Julius Baer Gruppe AG (BAER.VX)

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

Analyst: Sentoor Kanagasabapathy
Covered since November 8 2011



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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

12 Month Rating			Relative Rating		
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53%	37%	10%	10%	80%	10%
44%	43%	40%	48%	43%	45%

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