

# Banking Bubbles

## Euro Periphery Convergence

■ **Euro Periphery Convergence Closes Value Gap** — Rapid share price recovery in recent months in the Euro Area peripheral countries has led bank valuations in these recently crisis-stricken markets to converge with the winners in the recent global financial crisis. We estimate that bank market capitalisation to GDP is similar for Greece (c21%) and Australia (c25%) while Iberia and Ireland have converged with the Nordics (c15%). The value of the UK domestic sector, calculated based on Lloyds, has closed to Canadian levels. Italy remains the only major European market with an EM level of bank equity market capitalisation to GDP level (c10%): we continue to favour Italy among the European Peripheral banks.

■ **Fashionable and Unfashionable EM** — Indian, Philippines and Nigeria have relatively high expected GDP growth 2014-16E (c6%) and relatively low bank market capitalisations (c10%) of GDP. Buy-rated stocks in these countries include Axis Bank (AXBK.BO, Price Rs1389.7), Metrobank (MBT.PS, Price P80) and Zenith Bank (ZENITHB.LG, Price ₦20.15). Indonesia and Peru have a similar expected GDP growth rate as India and Philippines but have bank market value to GDP ratios 2-3x higher. China remains an outlier, with the highest bank earnings to GDP (c3%) but one of the lowest PE ratios, together with Russia, which also wins the prize for lowest bank market value to GDP (c4%).

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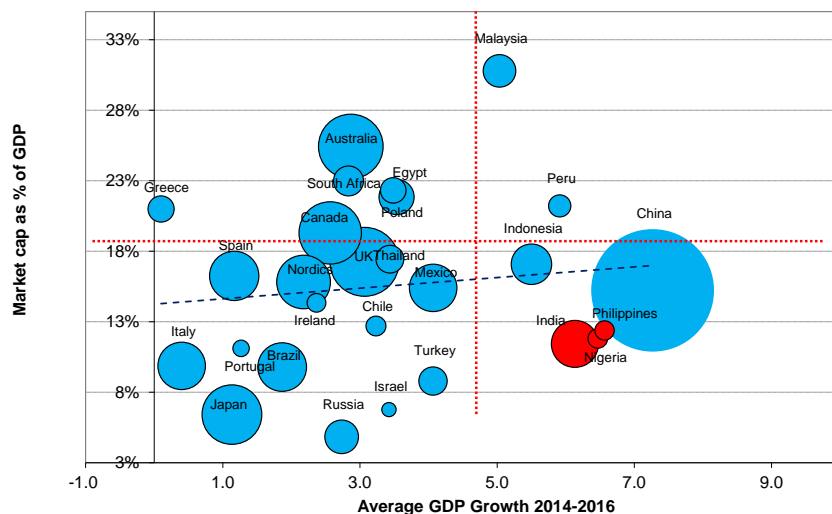
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Figure 1. Market Cap-to-GDP and GDP Growth 2014E-2016E (%)



Source: IMF, Company Reports and Citi Research. Size of the bubble in chart reflects bank sector market value. This is calculated based on domestic bank earnings for quoted banks covered by Citi Research and scaled up to estimate system equity value. The market value figures are based on estimation from a sample and not a reported figure.

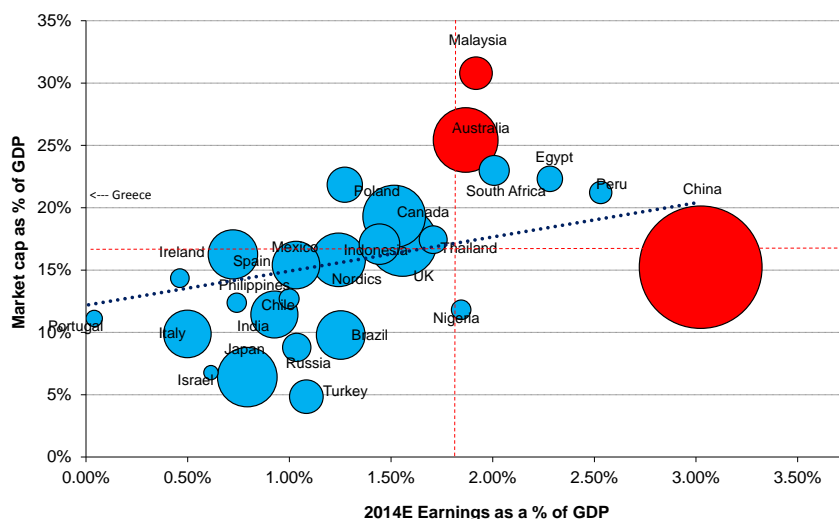
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China still leads the way on Bank Earnings/GDP (c3%); among larger markets, Australia, Malaysia also high up (c2%). "Low Earners" currently: Greece, Portugal, Ireland and Italy; for EM: Philippines and India.

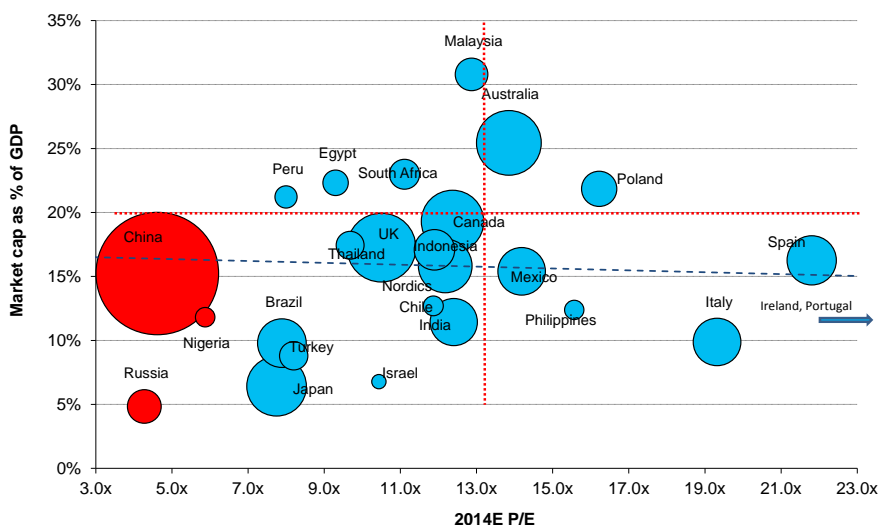
Figure 2. World Bank Sectors – Market Cap-to-GDP and 2014E Earnings-to-GDP (%)



Source: Company Reports and Citi Research. Size of the bubble in chart reflects bank sector market capitalisation

High EPS vs Low P/E: China. Low EPS vs Low P/E: Russia. High EPS vs High P/E: Australia. Low EPS vs High P/E: Mexico, Phils and Euro peripheries.

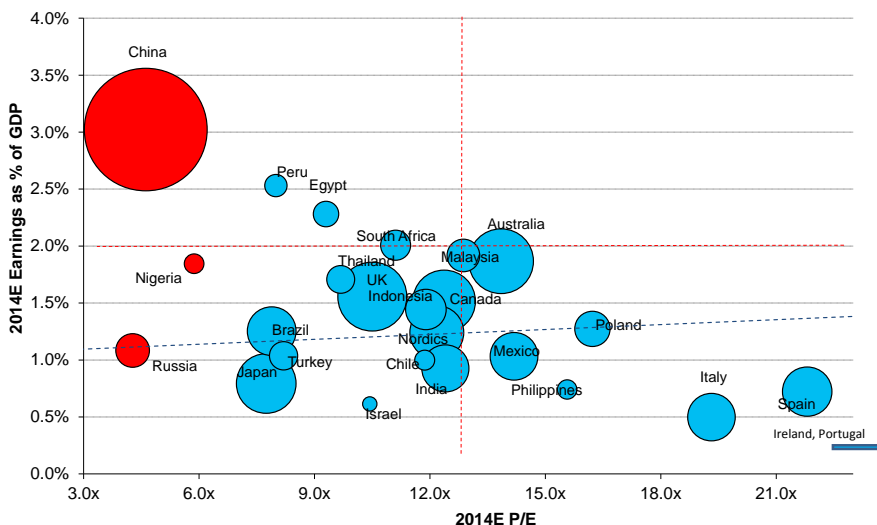
Figure 3. World Bank Sectors – Market Cap-to-GDP and 2014E P/E (%)



Source: Company Reports and Citi Research. Size of the bubble in chart reflects bank sector market capitalisation

Lowest PE rated bank sectors are Russia (4.3x) and China (4.6x) but with very different Bank Earnings/GDP (3.0% and 1.1%)

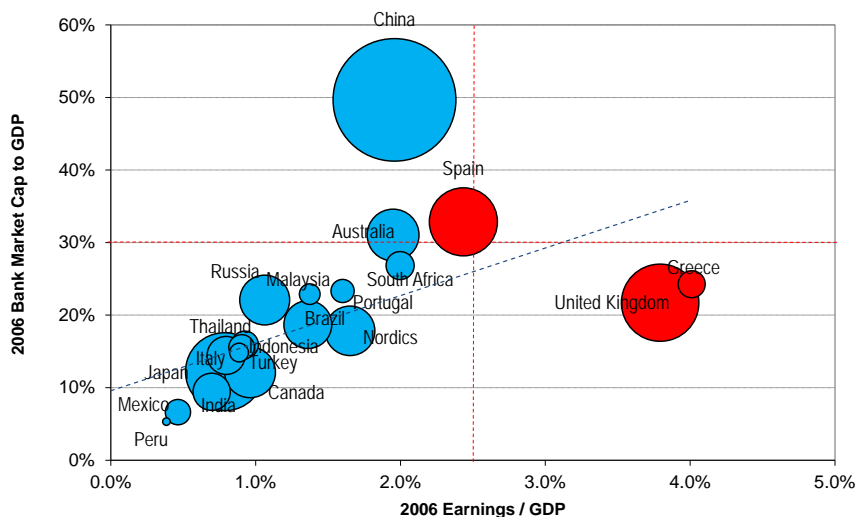
Figure 4. World Bank Sectors – 2014 Earnings-to-GDP and 2014E P/E (x)



Source: Company Reports and Citi Research. Size of the bubble in chart reflects bank sector market capitalisation

The banking world was different in 2006: Greece, UK, Spain and China led on earnings/GDP while China, Spain and Australia had high Market cap/GDP

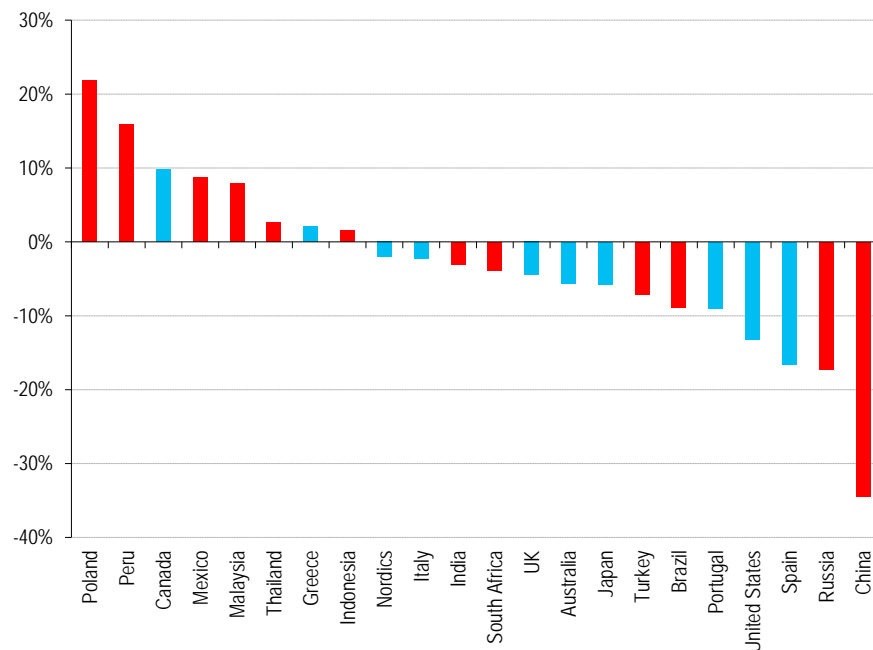
Figure 5. World Bank Sectors – 2006 Market Cap-to-GDP and 2006 Earnings-to-GDP (%)



Source: Company Reports and Citi Research. Size of the bubble in chart reflects bank sector market cap

**Banking system market cap to GDP lower now vs 2006: China, Russia, Spain lead Decliners. Other Losers: US, Portugal, Brazil. Relative winners: Poland, Peru, Canada, Mexico, Malaysia**

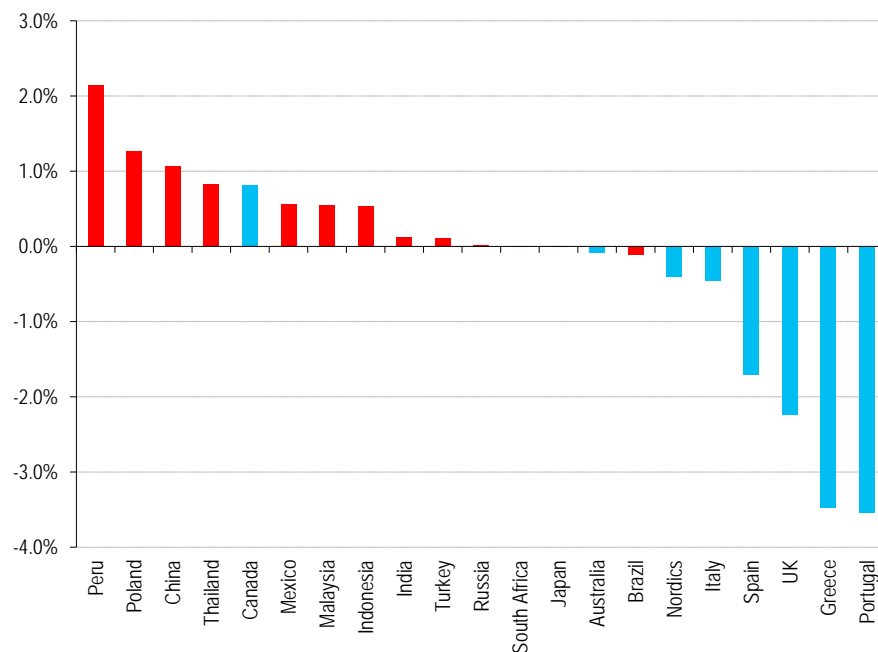
Figure 6. Banking System Market Cap-to-GDP – Current vs 2006 (%pt)



Source: IMF, Company Reports and Citi Research; Note: Red bars represent EMs while Blue represent DM economies

**Earnings to GDP trends mixed. Winners: Asean, China, Latin America (Spanish), Canada. Losers: Euro peripheries, UK, Nordics**

Figure 7. Banking System Earnings-to-GDP – 2014 vs 2006 (%pt)



Source: IMF, Company Reports and Citi Research; Note: Red bars represent EMs while Blue represent DM economies

## AXIS Bank

### Valuation

Our target price of Rs1,430 is based on a 1.6x 1yr Fwd P/BV (Dec'14E). While we believe that Axis should trade above government banks and in line with the multiples for large private-sector banks given its ROE, we recognize in the lower multiples potential over-hangs in Axis' most recent MSCI India exclusion, and the possibility of the government divesting its holding (SUUTI) of about 21%.

### Risks

Key downside risks to achieving our target price are: 1) Greater-than-expected asset quality pressures, as Axis has grown rapidly; 2) Sharp slowdown in rapidly growing fee income; 3) The bank's large share of wholesale funding could be exposed to tighter funding; 4) Dependence on treasury returns; 5) A government-related entity is a dominant shareholder in Axis; any disorderly sale would have an impact on the stock

## Metrobank

### Valuation

Our 12-month target price for Metrobank of P127 is based on a target P/BV of 2.0x, which is derived from a modified Gordon Growth model in which our key assumptions include 10.4% cost of equity (4.6% risk free rate, 5% risk premium, and beta of 1.15) and sustainable long term ROE of 11.8%. Our target P/BV is above MBT's historic P/BV of 1.3x, but we believed this is justified given improvement in tangible ROE that we expect until 2015.

### Risks

Downside risks include: (1) Slower-than-expected GDP growth that could weaken credit demand; (2) Sharp volatility in interest rates that could result in trading losses; (3) Banking regulatory changes, particularly more restrictive Basel 3 rules; and (4) Competitive pressures. Specific near-term earnings risks for Metrobank relate to slower than expected recovery in fee income, inability of MBT to generate the same returns from the non-financial assets it divested, further divestment of non-financial holdings and higher than expected growth in operating expenses resulting from more aggressive expansion program. Any of these risk factors could cause the shares to deviate from our target price.

## Zenith Bank Plc

### Valuation

Our fair value estimate and target price for Zenith Bank is NGN29. Our fair value estimate implies a target P/2013E BV and P/2014E EPS of 1.83x and 7.7x, respectively.

To calculate our fair value estimate for Zenith Bank we have applied our standard five-year dividend discount model. The cost of equity assumed is 17% and this has been derived using a risk free rate of 11%, equity risk premium of 6.0% and a beta of 1.0x. We apply a 6% terminal growth rate to all the Nigerian banks.

## **Risks**

The risks to Zenith Bank's share price reaching our target price could come in our view from the following: (i) global economic correction on the back of the European debt crisis, which could put pressure on crude oil prices; (ii) asset yield risks on the back of increased lending to high-end corporates; and (iii) liquidity risks associated with surpluses being built up on bank balance sheets, which could result in poor lending practices.

# Appendix A-1

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#### Ratings and Target Price History Fundamental Research

Analyst: Simon Nellis

Covered since September 16 2013



	Date	Rating	Target Price	Closing Price
1	4-May-11	1L	*20.00	15.35
2	7-Oct-11	Stock rating system changed		

\* Indicates change

	Date	Rating	Target Price	Closing Price
3	7-Oct-11	*1	20.00	12.10
4	22-May-12	1	*21.00	14.88

	Date	Rating	Target Price	Closing Price
5	11-Jan-13	1	*26.00	20.13
6	17-Apr-13	1	*29.00	19.40

Rating/target price changes above reflect Eastern Standard Time

### Zenith Bank Plc (ZENITHB.LG)

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

Analyst: Simon Nellis

Covered since September 16 2013



	Date	Rating	Target Price	Closing Price
1	13-Jul-11	*ADD MP	-	14.03

\* Indicates change

	Date	Rating	Target Price	Closing Price
2	18-Oct-11	*REM MP	-	12.20

Rating/target price changes above reflect Eastern Standard Time

## AXIS Bank (AXBK.BO)

### Ratings and Target Price History

### Fundamental Research

Analyst: Aditya Narain, CFA  
Covered since March 26 2012



	Date	Rating	Target Price	Closing Price
1	26-Sep-11	1L	*1,400.00	1,055.80
2	7-Oct-11	Stock rating system changed		
3	7-Oct-11	*1	1,400.00	1,029.95

\* Indicates change

	Date	Rating	Target Price	Closing Price
4	22-Jan-12	1	*1,320.00	1,008.00
5	9-Oct-12	1	*1,433.00	1,128.20
6	15-Jan-13	1	*1,615.00	1,422.45

	Date	Rating	Target Price	Closing Price
7	23-May-13	1	*1,795.00	1,455.50
8	28-Aug-13	1	*1,080.00	838.70
9	4-Dec-13	1	*1,430.00	1,189.70

Rating/target price changes above reflect Eastern Standard Time

## AXIS Bank (AXBK.BO)

### Ratings and Target Price History

### Best Ideas Research

### Relative Call (3 Month)

Analyst: Aditya Narain, CFA  
Covered since March 26 2012



	Date	Rating	Target Price	Closing Price
1	9-Apr-12	*REM MP	-	1,144.10
2	30-Jun-12	*N	-	1,015.80

\* Indicates change

	Date	Rating	Target Price	Closing Price
3	13-Jul-12	*ADD MP	-	1,034.85
4	6-Nov-13	*REM MP	-	1,212.00

Rating/target price changes above reflect Eastern Standard Time

## Metrobank (MBT.PS)

### Ratings and Target Price History

### Fundamental Research

Analyst: Minda A. Olanon  
Covered since April 12 2011



	Date	Rating	Target Price	Closing Price
1	12-Apr-11	*1L	*59.23	51.54
2	9-Jun-11	1L	*63.08	54.38
3	16-Aug-11	1L	*66.15	57.19

\* Indicates change

	Date	Rating	Target Price	Closing Price
4	7-Oct-11	Stock rating system changed		
5	7-Oct-11	*1	66.15	49.88
6	27-Mar-12	1	*79.23	67.69

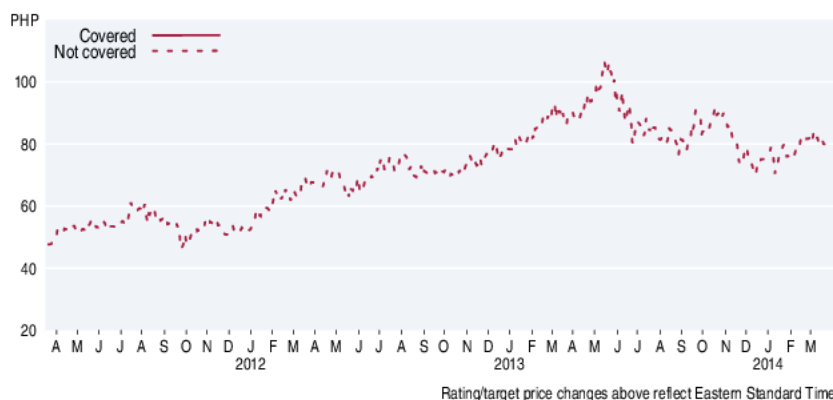
	Date	Rating	Target Price	Closing Price
7	4-Sep-12	*2	*76.92	71.15
8	30-Jan-13	2	*88.46	82.00
9	12-Aug-13	*1	*97.69	80.69

Rating/target price changes above reflect Eastern Standard Time



**Metrobank (MBT.PS)**  
**Ratings and Target Price History**  
**Best Ideas Research**  
**Relative Call (3 Month)**

Analyst: Minda A. Olanan  
Covered since April 12 2011



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*Data current as of 31 Dec 2013*

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	Buy	Hold	Sell	Buy	Hold	Sell
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% of companies in each rating category that are investment banking clients	55%	52%	44%	62%	52%	49%

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