

Financial Institutions

Sector Review – November & December



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1. Sector Overview

- The months of November and December were defined by two main events. First and foremost, we witnessed the beginning of Quantitative Easing tapering, with the Fed reducing the pace of monthly bond purchases from \$85 bn to \$75 bn, while Bernanke said that the Fed would be likely to maintain interest rates low until the unemployment rate falls significantly, which helped to reduce the effect of the announcement. Despite this, in the analyzed period the US 10 year yield increased by 50 bps closing the year around 3%.
- With Janet Yellen taking over as the next chair of Federal Reserve we expect further tapering for 2014 which could lead to financial institutions underperforming in the next year.
- The second major event has to do with further capital regulations, with higher leverage ratio requirements under Basel III and the final approval of the Volcker rule, which bans banks risky proprietary trading. All of the regulation introduced in the past years have produced large transformations in the sector, hurting banks' profitability while, on the other hand, strengthening their balance sheets and making them safer investments.

Financial Institutions Universe:

- Goldman Sachs
- BCP
- BNP Paribas
- HSBC
- AIG

This month's detailed company review:

- Goldman Sachs



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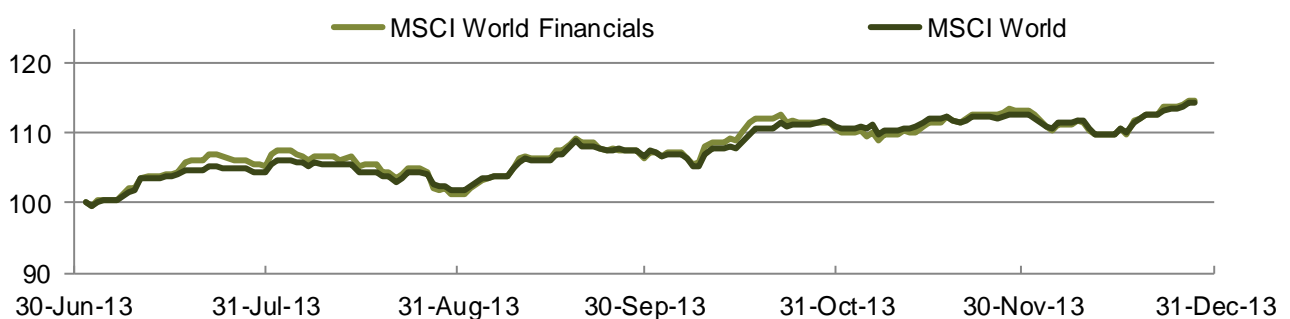


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Financial Institutions Sector vs. Overall market



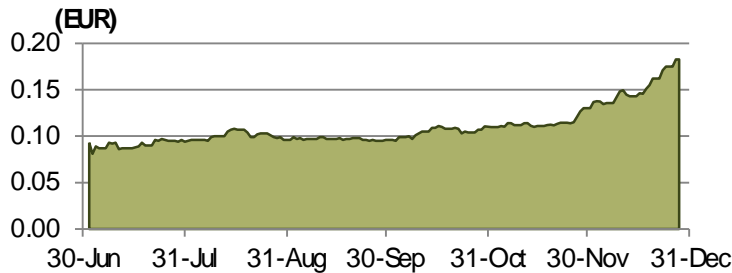
- During the considered six months period, the chosen indexes that represent both the Global Financial Institution's market and Global equity market followed a very similar path. Economic forecasts for 2014 are more optimistic than they have been in years and if these prove accurate, financial institutions will have more business to compete for. Nevertheless they will also have to cope with low levels of trust caused by scandals such as the Libor-fixing.

2. Followed Companies

BCP

(Ticker: BCP PL)

- In the beginning of November, Millennium BCP posted a slightly better-than-expected nine-month-loss caused mainly by impairments on problematic loans originated at home and in Greece and by the cost of using a recapitalization line. The net loss was equal to 597 million euros, which is better than the 612 million euros forecasted by analysts.

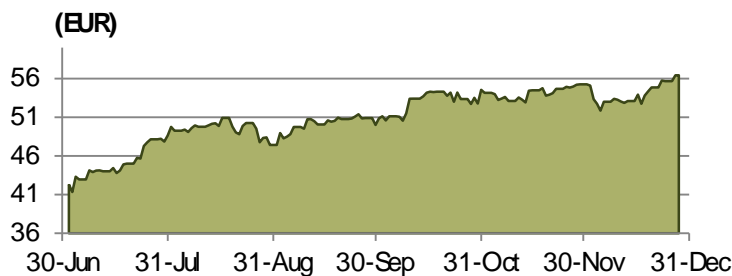


Price (EUR):	→	0.18
Target Price (EUR):		0.19
Up/ downside:		4.0%
Performance 3M:		92.3%
P/ E Ratio:		
ROC/ WACC:		0.2x

BNP Paribas

(Ticker: BNP FP)

- BNP Paribas has agreed to buy the Polish business of its Dutch rival Rabobank for \$1.4 billion. This deal still needs the approval from Poland's banking regulator KNF. Due to the existence of this deal, BNP Paribas has suspended the preparation for a share issue of its Polish unit, which needs to raise its free float to 15 percent due to regulatory restrictions.

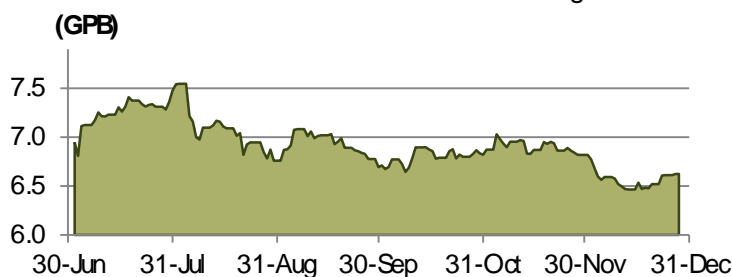


Price (EUR):	↑	56.42
Target Price (EUR):		63.00
Up/ downside:		11.7%
Performance 3M:		10.9%
P/ E Ratio:		13.9x
ROC/ WACC:		0.7x

HSBC

(Ticker: HSBA LN)

- HSBC reported an underlying pretax profit for the third quarter of \$5.1 billion. These profits were registered mainly due to tighter cost controls, but also due to fewer losses from bad loans. Strong performance in the Hong Kong and British markets together accounts for more than half of the earnings.

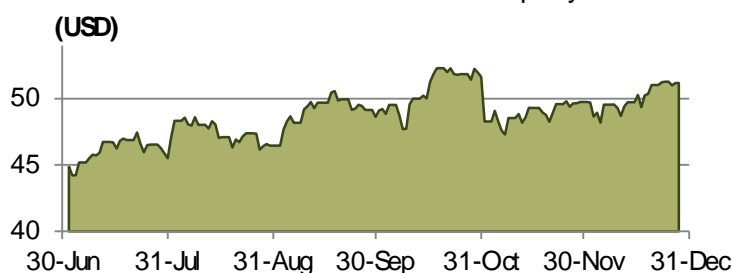


Price (GBP):	↑	6.62
Target Price (GBP):		7.73
Up/ downside:		16.6%
Performance 3M:		-2.3%
P/ E Ratio:		11.4x
ROC/ WACC:		0.8x

AIG

(Ticker: AIG US)

- In December AIG announced that it will sell its aircraft-leasing business to AerCap Holdings NV for \$5.4 billion. This announcement marks the probable end of a four-year effort performed by AIG to divest its biggest non-insurance business. AIG hopes that the sale of this branch will allow the company to focus on its insurance activities.



Price (EUR):	↑	51.18
Target Price (EUR):		58.00
Up/ downside:		13.3%
Performance 3M:		4.1%
P/ E Ratio:		13.5x
ROC/ WACC:		0.3x

3. Stock Analysis: Goldman Sachs

Corporate News

- Fourth quarter net revenues of the trading division of Goldman Sachs fell by 15% to \$1.72 billion in 2013 from \$2 billion in the fourth quarter of 2012. At the end of December, the trading unit registered losses on 15 consecutive days, the most since 2011. In total, revenues generated by the trading unit fell 13% to \$8.65 billion in 2013 from \$9.91 billion in 2012. However, thanks to cost cuts and repurchases of shares, Goldman Sachs was able to increase the earnings per share on 2013 by \$1.33 and have a return on equity equal to 11%.

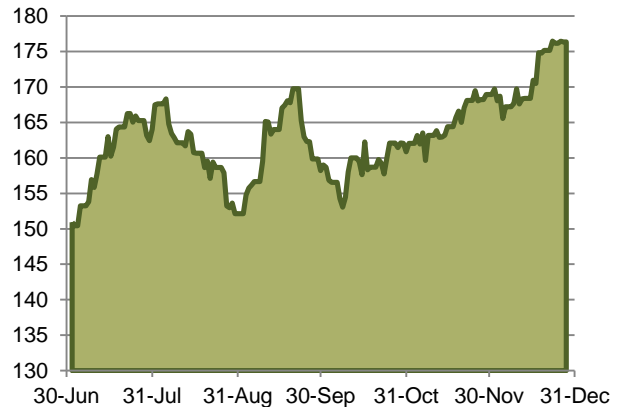
Market Performance

- In the past two months, Goldman Sachs' stock price has increased from \$160.86 to \$177.26, showing a 10.2% increase in value. This performance is very encouraging specially if it is taken into account the fact that returns for the S&P500 index in this period were equal to approximately 5.23%.
- Besides performing better than the market, Goldman Sachs also performed better than its direct peers chosen for this report. HSBC's shares suffered a loss in value equal to 1.35% in the past 2 months, and BNP Paribas saw the value of its shares increase by a modest 3.87%.

Valuation Summary

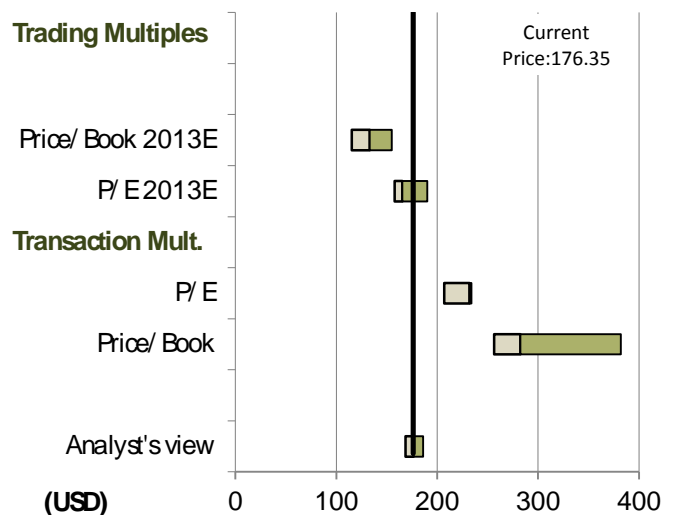
- Looking at the valuation summary, we can say that Goldman Sachs appears to be fairly valued. According to the Price/Book and P/E Goldman Sachs is slightly overpriced but if we look at the analysts' consensus we can see that the general consensus is that the firm is fully valued. These results are consistent with the transaction multiples, which seem to indicate that the company is undervalued, as expected since these include a control premium typical in M&A deals. This supports the idea that financials may become the new Consumer Staples since, due to capital requirements, growth expectations are lower and banks are viewed as a relatively safe investments

(USD) Stock Performance



Goldman Sachs (USD)	
Current Price (28/ 12/ 2013)	176.35
52-week high % change	-2.6%
Median Target Price	179.61
Market Capitalisation (mm)	77,983
Return on Common Equity	12.0%
Dividend Yield	1.2%
Beta (vs S&P500)	1.6x
Total Debt/ Equity	670.0%

Valuation Summary (Price per Share)



Comparable Analysis

Company Name	Currency	M Cap (mn)	e Value (mn)	Price/Book			ROE			P/E		
				LTM	2013E	2014E	LTM	2013E	2014E	LTM	2013E	2014E
Goldman Sachs	USD	77,983	521,882	1.1x	1.0x	0.9x	12.0%	10.3%	10.2%	9.6x	10.4x	9.7x
Citigroup	USD	146,310	770,998	0.7x	0.7x	0.6x	7.1%	7.6%	8.0%	9.8x	9.6x	8.3x
Bank of America	USD	179,319	N/A	0.8x	0.8x	0.7x	4.6%	6.8%	7.6%	11.1x	12.3x	10.2x
J.P. Morgan	USD	210,342	N/A	1.1x	1.0x	0.9x	8.4%	10.9%	10.7%	15.4x	9.4x	8.8x
Deutsche Bank	EUR	36,192	N/A	0.6x	0.6x	0.6x	-0.9%	6.2%	8.3%	23.9x	9.8x	7.2x
Morgan Stanley	USD	57,529	495,646	0.9x	0.9x	0.8x	5.0%	7.5%	8.5%	14.4x	12.0x	10.0x
75th Percentile				1.0x	0.9x	0.9x	8.1%	9.6%	9.8%	14.4x	11.6x	9.9x
Median				0.9x	0.8x	0.8x	6.1%	7.5%	8.4%	11.1x	10.1x	9.2x
25th Percentile				0.8x	0.7x	0.7x	4.7%	6.9%	8.1%	9.8x	9.6x	8.5x

- As we mentioned previously, examining the comparable companies trading multiples, Goldman Sachs seems to be fully valued, especially if we look at its P/E ratio in 2013, 10.4x, which is fairly close to the comparable firms median (10.1x). An analysis of the Price/Book ratios would indicate that Goldman is slightly overvalued (0.8x vs 1.0x in 2013), but when we examine Goldman's most direct competitors, as a "pure" investment bank (JP Morgan and Morgan Stanley), the Price/Book ratios are fairly closer (1.0x and 0.9x respectively). Historically, Goldman's Price/Book ratio has slightly higher but since the 2008 crisis and introduction of restrictions on proprietary trading this metric has been on decline. However, if we use boutique banks as a comparison, which have never relied on prop trading, we see that Goldman could trade at significantly higher multiples, given a change in business mix.

Precedent Transactions

Announced Date	Target		Buyer		EV (EUR mn)	P/E	Price/Book
	Company	Country	Company	Country			
05-Dec-13	Bank Gospodarki Zywosciowej SA	PL	BNP Paribas SA	FR	1,002	22.5x	1.1x
02-Jul-13	Bank of Ayudhya	TH	Mitsubishi UFJ Financial Group	JP	4,229	14.0x	1.5x
28-Sep-12	Denizbank AS	TR	Sberbank of Russia	RU	2,836	12.4x	1.5x
02-Nov-10	Turkiye Garanti Bankasi AS	TR	BBVA SA	SP	2,690	11.0x	1.7x
09-Oct-10	Bank Zachodni WBK SA	PL	Banco Santander SA	SP	4,207	13.9x	2.3x
09-Jun-10	Grupo Financiero Santander Mexico	MX	Banco Santander SA	SP	2,078	15.3x	2.8x
75th Percentile						14.0x	2.3x
Median						13.9x	1.7x
25th Percentile						12.4x	1.5x

- For this report we chose to make some changes in the precedent transaction table by replacing three of the older deals (2008 and 2009) by two more recent ones (2013) since we were concerned that the previous set of transactions might not be representative of the current state of the sector. The chosen deals were the acquisition of Bank of Ayudhya by Mitsubishi UFJ, in an expansion effort by the Japanese in Thailand, the second largest economy in Southeast Asia; and the acquisition of BGZ by BNP Paribas from Rabobank for €1 bn in what was one of the largest deals in Europe within the financial sector. Both deals were for a controlling stake in the companies.
- Looking more closely to the median multiples in comparison to the trading multiples above we can see that these evidently reflect the control premiums included in the transaction value as well as possible synergies given that we are analyzing cross border deals – 13.9x vs. 10.1x for P/E multiples and 1.7x vs. 0.8x for Price/Book. These valuation metrics would put a price on Goldman of anywhere between \$230 to \$280, more than 30% more than its current value.