

Financial Institutions

Sector Review – September & October



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1. Sector Overview

- The trend in litigation that we saw during the summer continues into the months of September and October with J.P. Morgan's practices continuing to be called into question. Under chief executive Jamie Dimon, the American bank has, yet again, reached a new deal with the federal government to pay \$13 billion to resolve the alleged mis-selling of mortgage-backed securities (MBS's). In fact, we have seen both J.P. Morgan and Deutsche Bank increasing their litigation reserves in their latest 3Q investor conferences.
- In Europe, banks expectations of a potential cut in interest rates, by up to 25 bps, in the euro zone have increased, as inflation decreased to 0.7%. This could potentially mean lower financing costs for banks, as banks continue to deleverage in order to meet Basel III demands.
- In contrast, corporate loan supply in Europe fell by 10% in September and, in a recent report by Fitch Ratings, sovereign debt holdings have increased by €550 billion among top European banks which coincided with a €440 billion drop in corporate loans.
- In the US, the government has tried to boost the real estate market, through refinancing originations and low mortgage rates, but this trend is expected to stop as the FED continues to considering tapering.

Financial Institutions Universe:

- BCP
- J.P. Morgan
- BNP Paribas
- HSBC
- AIG

This month's detailed company review:

- J.P. Morgan



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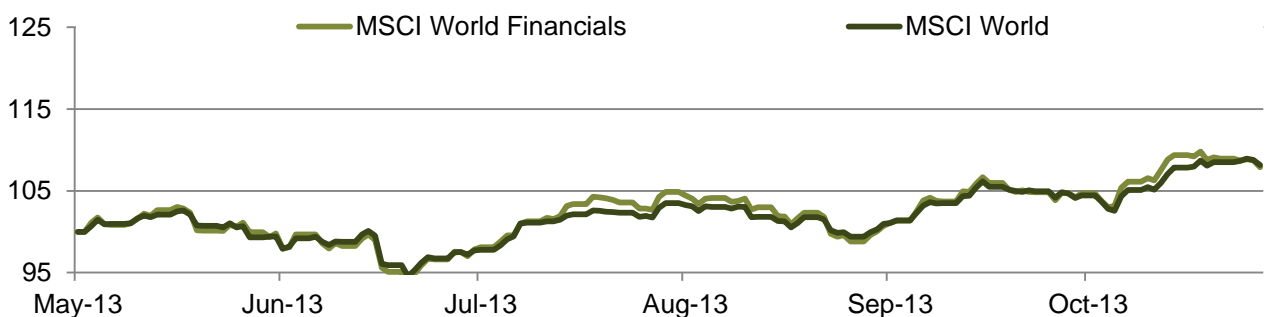


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Financial Institutions Sector vs. Overall market



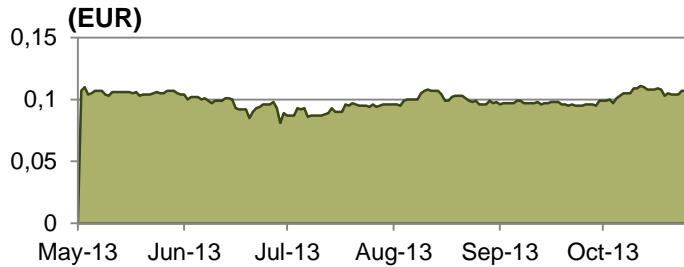
- During the considered six months period, the chosen indexes that represent both the Global Financial Institution's market and Global equity market followed a very similar path. There is a positive outlook for financial institutions in the next few months mainly due to the fact that GDP in the U.S. is steadily growing again, but regulatory-related matters and low levels of trust are definitely going to have a negative effect on this sector's performance.

2. Followed Companies

BCP

(Ticker: BCP PL)

- At the end of October, Millennium BCP divested its 4.64% stake on in Greece's Piraeus bank in an accelerated placement to institutional investors. This stake was acquired in April for 400 million euros as part of BCP's deal to sell its Greek unit, Millennium Bank-Greece.

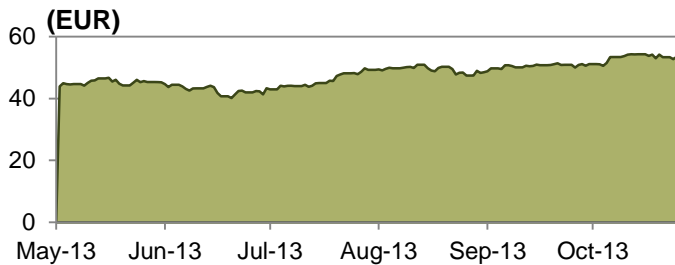


Price (EUR):	→	0,11
Target Price (EUR):		0,11
Up/downside:		-0,2%
Performance 3M:		17,2%
P/E Ratio:		N/A
ROC/WACC:		0,1x

BNP Paribas

(Ticker: BNP FP)

- In an effort to appease regulators and to protect profits from the financial crisis and fragile economic recovery, BNP has pledged to save \$2.70 billion a year by 2015 through a cost-cutting drive, while at the same time reinvesting to grow beyond its core markets.

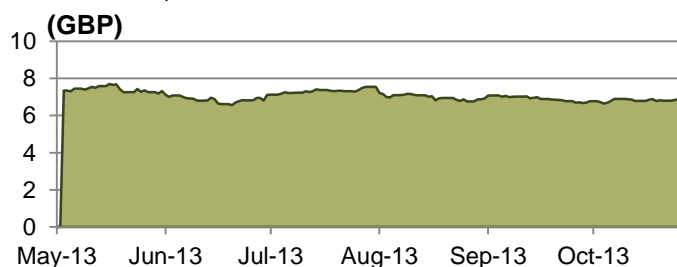


Price (EUR):	↑	54,54
Target Price (EUR):		60,00
Up/downside:		10,0%
Performance 3M:		12,1%
P/E Ratio:		13,3x
ROC/WACC:		0,6x

HSBC

(Ticker: HSBA LN)

- HSBC's net profit in the third quarter of this year rose 28% when compared to the same period of the last year. Revenue for the British giant was fairly stable but costs as a proportion of revenue (excluding gains and losses in the value of the bank's own debt), fell to 61% from 64%.

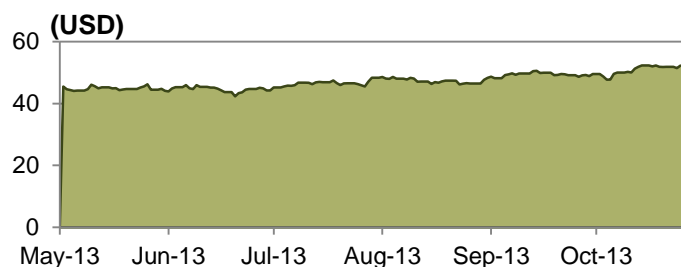


Price (GBP):	↑	6,82
Target Price (GBP):		7,75
Up/downside:		13,6%
Performance 3M:		-9,6%
P/E Ratio:		12,5x
ROC/WACC:		0,8x

AIG

(Ticker: AIG US)

- AIG has ended the \$182.3 billion U.S. rescue in December of 2012, in part by repurchasing its own shares, and is now working to improve margins at the property-casualty unit (AIG's largest division) and expand sales to consumers.



Price (USD):	↑	51,65
Target Price (USD):		55,00
Up/downside:		6,5%
Performance 3M:		13,5%
P/E Ratio:		13,4x
ROC/WACC:		0,3x

3. Stock Analysis: J.P. Morgan

Corporate News

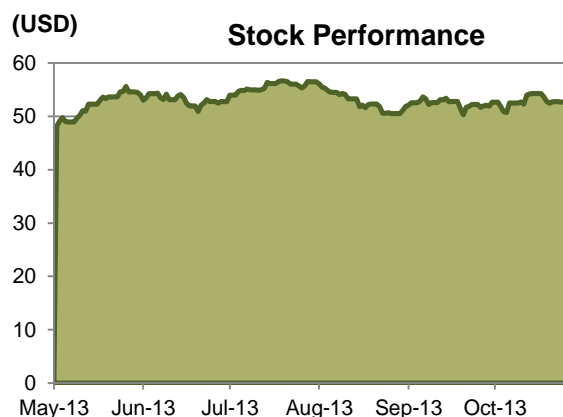
- On the 26th of October J.P. Morgan reached a \$5.1 billion settlement with the U.S. mortgage company regulator. The deal settles a lawsuit brought by Federal Housing Finance Agency (FHFA), which regulates government-backed loan firms Fannie Mae and Freddie Mac. The FHFA alleged J.P. Morgan misled Fannie and Freddie about the quality of mortgages it sold to them during the housing boom. The value that J.P Morgan is going to pay to FHFA is part of a preliminary \$13 billion tentative deal that has been settled with US justice.

Market Performance

- In the past two months, J.P. Morgan's' stock price has stayed fairly stable at \$51, showing a 0.8% increase in value. Analysing excess returns on the market benchmark (S&P500), the results are not very positive as the S&P500 returned 7% on the period under analysis.
- However, when we compare the company with its peers we can see that J.P. Morgan has actually outperformed them, in terms of variation in stock price. For example, Bank of America and Citigroup's price performances, were -2% and -1.2% respectively. Therefore, despite the poor performance relative to the market index, we can conclude that J.P. Morgan was still above average within the FIG sector.

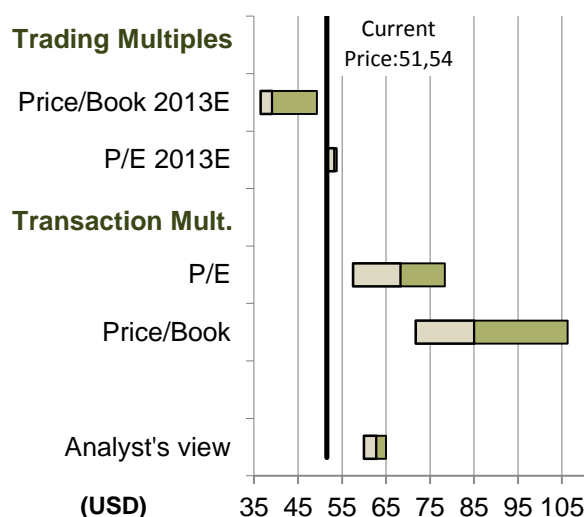
Valuation Summary

- Examining the valuation multiples, we can conclude that J.P. Morgan appears to be correctly priced according to trading multiples, while somewhat undervalued if we use transaction multiples (both P/B and P/E). Still, given that transaction multiples have an implied control premium this type of behavior would be expected. Lastly, if we use analysts' price forecasts we get a median price of \$62.8 which is more in line with the median target price (\$61.7). Hence, we expect the stock's price to increase in the coming months from its current price (\$51.54).



J.P. Morgan (USD)	
Current Price (31/10/2013)	51,54
52-week high % change	-9,5%
Median Target Price	61,70
Market Capitalisation (mn)	197.395
Return on Common Equity	8,8%
Dividend Yield	2,6%
Beta (vs. S&P500)	1,5x
Total Debt/Equity	340,9%

Valuation Summary (Price per Share)



Comparable Analysis

Company Name	Currency	MCap (mn)	e Value (mn)	Price/Book			ROE			P/E		
				LTM	2013E	2014E	LTM	2013E	2014E	LTM	2013E	2014E
J.P. Morgan	USD	197.395	N/A	1,0x	1,0x	0,9x	8,8x	9,4x	11,0x	8,1x	10,9x	8,7x
Citigroup	USD	147.828	747.935	0,8x	0,7x	0,7x	6,4x	7,4x	8,0x	9,8x	10,3x	9,0x
Bank of America	USD	149.539	N/A	0,7x	0,7x	0,6x	3,3x	4,7x	6,7x	9,8x	14,9x	10,3x
Goldman Sachs	USD	75.697	524.512	1,1x	1,1x	1,0x	12,0x	10,5x	10,0x	15,4x	10,8x	10,5x
Deutsche Bank	EUR	35.846	N/A	0,6x	0,6x	0,6x	-0,9x	5,2x	7,0x	43,0x	11,0x	8,2x
Barclays	GBp	41.425	N/A	0,7x	0,7x	0,7x	1,3x	5,6x	8,3x	N/A	9,8x	8,3x
75th Percentile				0,9x	0,9x	0,9x	8,2x	8,9x	9,6x	18,1x	11,0x	10,0x
Median				0,7x	0,7x	0,7x	4,9x	6,5x	8,1x	9,8x	10,8x	8,8x
25th Percentile				0,7x	0,7x	0,6x	1,8x	5,3x	7,3x	9,4x	10,5x	8,4x

- Looking at the comparable companies, it is relevant to compare J.P. Morgan's trading multiples both with its competitors and the industry median. The P/E trading multiple of the industry (10.8x) shows that J.P. Morgan is slightly overvalued (10.9x). By analyzing the Price/Book trading multiple, it is possible to see that the company's overvaluation is slightly higher than in the previous case (1.0x versus an industry value equal to 0.7x).
- Regarding the relationship with two of its main competitors, Citigroup and Bank of America, the Price/Book multiple reflects the same assessment presented above. The same can't be said about the P/E multiple, which shows Bank of America as the most overvalued bank of the group.

Precedent Transactions

Announced Date	Target		Buyer		EV (EUR mn)	P/E	Price/Book
	Company	Country	Company	Country			
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
31-Jul-09	Resona Holdings Inc	JP	Bank of America Corp	US	769	3.6x	1.0x
20-Oct-08	Bank Ekonomi Raharja Tbk	ID	HSBC Holdings PLC	UK	446	20.9x	1.6x
12-Sep-08	Deutsche Postbank AG	GR	Deutsche Bank AG	GR	2,700	16.6x	1.2x
75th Percentile						16.0x	2.0x
Median						13.9x	1.6x
25th Percentile						11.7x	1.4x

- In order to compute the transaction multiples we chose 7 deals over a 5 year period, given the low activity in the M&A market for the past couple of years, that we believe to be representative of the industry on a global perspective, taking into account region and transaction value .
- The most significant transaction that happened in the last five years, within the European market and with disclosed multiples, was when Banco Santander bought a stake of Bank Zachodni WBK SA. The presented multiples for this transaction are fairly in line with the ones of Barclays. Again, in regards to the P/E multiple the British bank appears to be slightly undervalued, while when considering Price/Book the undervaluation is even clearer. These results would hold even when taking into account the paid control premium.
- The most recent transaction happened in the third quarter of the last year, between a Russian (Sberbank) and Turkish (Denizbank) bank. This is indicative of the low frequency of deals recently, as well as a lack of significant deals between larger banks in the past years.