

- We upgrade our rating to Neutral from Sell, with TP slightly down to PLN 441 from PLN 443
- We cut our adjusted net profit estimates by 11% in 2018E and by 10% in 2019E.

Upgrade to Neutral after the share price drop.

We trim our 12M TP for mBank to PLN 441 from PLN 443 previously, but due to share price drop we upgrade our rating to Neutral (from Sell). Sale of an organized part of mFinanse coupled with 1Q18E results and changes in expected interest rates cuts prompted us to cut our earnings estimates for mBank by 11/10% in 2018/19E. Our forecasts are 5% below consensus, that – in our view – does not fully reflect revenues lost due to sale of mFinanse. Due to poor NIM-CoR profile mBank remains one of the least profitable banks in our coverage (in 2018/19E we expect 8.0/8.6% ROE vs. 9.6/10.5% sector median). However, it offers decent EPS growth (9/15% YoY in 2018/19E), is capable to pay dividend and has been continuously reducing its FX mortgage exposure. Thus, we see its current valuation at 15.6x 2018E P/E and 1.2x P/BV as fair. In this note we present also 1Q18E preview for all the 9 banks in our coverage.

1Q18 driven by one-off. We expect mBank to report 1Q18 net profit of PLN 377m (72% YoY) driven by one-off gain on sale of mFinanse. We expect adjusted earnings though to drop 6% YoY (to PLN 287m) negatively affected by higher provisions (74% YoY) and costs (5% YoY) that should more than offset strong NII (10% YoY) and F&C (5% YoY).

We cut our 2018/19E estimates by 11/10%. Sales of mFinanse coupled with 4Q17 results and changes in expected interest rates cuts (we now assume 25bp hike in 4Q19 vs. 2x25bp in 3/4Q18 previously) prompted us to cut our earnings estimates by 11% in 2018E and by 10% in 2019E. Our 2018/19E forecasts are 5% below consensus.

We expect downgrades in consensus estimates. In March 2018 mBank finalized sale of an organized part of mFinanse. The bank expects to report PLN 177m one-off gain in 1Q18 and up to PLN 190m spread over the next 6 years. According to our estimates the sold part of mFinanse added to mBank's 2017 consolidated revenues c. PLN 90m (10% of net fee income). However, starting in 2Q18 it will no longer support the bank's revenues, what - in our view – is yet not fully reflected in consensus estimates.

Valuation sounds fair. At our forecasts mBank is trading at 15.6x 2018E P/E and 1.2x P/BV, with 4% premium and 10% discount to peers, respectively. Given expected EPS growth on one hand and below average profitability on the other hand, we see its current valuation as fair.

CHF risk declining, but still on. While mBank has been successfully reducing its FX mortgage risk, with 21% share of FX mortgages in total loans it remains one of the most exposed Polish banks. We maintain our assumption of PLN 4.8bn FX conversion sector cost resulting from a quarterly contribution at 0.2% of FX loan book, that would consume c. 13% of net profit in the first year and 4% of BV over the next 5 years.

Figure 1. mBank – Key data, 2015-2020E

	2015	2016	2017	2018E	2019E	2020E
Adjusted net profit (PLNm)	1 180	996	1 092	1 191	1 371	1 504
YoY change (%)	-8%	-16%	10%	9%	15%	10%
Adjusted ROE (%)	10.1%	7.9%	8.0%	8.0%	8.6%	8.9%
P/E (x) adjusted	15.7	18.6	17.0	15.6	13.6	12.4
P/BV (x)	1.5	1.4	1.3	1.2	1.1	1.1
DPS* (PLN)	0.0	0.0	5.1	9.9	13.3	14.6
DY* (%)	0.0%	0.0%	1.2%	2.3%	3.0%	3.3%

* from the year's earnings. Source: Company data, Vestor DM estimates

Company data

Rating	Neutral
Target Price (PLN)	441.0
Market Price (PLN)	439.2
Upside/downside	0%
Previous rating	Sell
Previous Target Price (PLN)	443.0
Min (52W)	372.7
Max (52W)	538.0
Market cap (PLNm)	18,583
Avg. 3M Turnover (PLNm)	7.8

Shareholders

	%
Commerzbank AG	69.4%
Other	30.6%

Company description

mBank is the fourth largest bank in Poland with almost 7% market share in assets and 271 branches. The bank has a strong exposure to corporate loans (44% of the loan book) and FX mortgage loans (21% vs. 17% PLN mortgage loans). Consumer loans constitute 15% of mBank's loan book.

mBank vs. WIG vs. WIG Banks 12M relative price performance rebased



Source: Bloomberg, Vestor DM

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A description of the organization mechanisms of Chinese walls aimed to prevent the conflicts of interest:

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- ii. supervising their own transactions made by individuals, periodic inspection and assessment of the effectiveness of implemented by Vestor control systems and procedures; conducting the legally required registers and records, primarily registry conflicts of interest associated with a significant risk of damage to client interests;

d) Refusal of action: the right to refuse the Vestor activity to the client, if given the commitment to specific activity on behalf of another client Vestor cannot effectively manage potential conflicts of interest, or prevent this regulatory restrictions or internal regulations;

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In preparing this document Vestor applied at least two of the following valuation methods:

- 1) Discounted cash flows (DCF),
- 2) Comparative valuation (including ROE-p/BV model),
- 3) Target multiple,
- 4) Scenario analysis,

- 5) Dividend discount model (DDM),
- 6) net asset value (NAV),
- 7) Sum of the parts,
- 8) Discounted residual income model (DRIM),
- 9) Risk-adjusted net present value (rNPV).

The discounted cash flows valuation method (DCF) is based on discounted expected future cash flows. The method includes all cash flows the issuer is expected to generate in a given period and the cost of money over time. However, the DCF valuation method requires a number of assumptions and is very sensitive to changes in parameters used in the model. Small changes in assumptions may result in material changes in the valuation.

The comparative valuation method is based on the rule of "one price". The advantages of the method include 1) a small number of parameters to be estimated, 2) the fact that there is a relatively large number of indicators for companies being compared, 3) The method is well-known among investors, 4) valuation is based on current market conditions. On the other hand, a comparative valuation is strongly sensitive to the valuation of the companies classified as peers and may lead to a simplified picture of the company valued.

The target multiple valuation approach is based on the assumption that the value of the company should be equal to pre-specified values of selected price multiples. The advantage of this method is its simplicity and applicability to almost all of the companies. The target multiple approach is a highly subjective method, though.

The scenario analysis approach is based on the probability weighted valuation for three sets of assumptions: Bear case, base case and bull case with a different probability assigned. The base case is based on the assumptions included in financial forecasts and DCF valuation. The bear/bull case scenarios present a sensitivity towards negative/positive changes in various assumptions including market size, market shares, profitability, growth, capex, valuation multiples etc. The advantage of this method is presentation of various scenarios and valuation sensitivity. A complexity and sensitivity to probability weights assumption may be found as disadvantages.

The dividend discount model (DDM) valuation is based on discounted future dividends that are expected to be paid out by the company over a period of time. The DDM model includes real cash streams that are expected to be received by shareholders and may be applied to companies with long-term dividend payout history. However, the DDM valuation method requires a number of assumptions.

The net asset value (NAV) approach considers the underlying value of the company's individual assets net of its liabilities. Among the advantages of the NAV approach are its applicability to asset holding companies and the fact that data required are usually easy to reach. On the other hand the NAV approach does not take into account future changes in revenues or income and can underestimate the value of intangible assets.

The sum of the parts approach values a company on the back of valuations of its separate divisions. The method is applicable to companies with very different business profiles, but requires identification of peers for business divisions comparison, what may be difficult to achieve.

The discounted residual income model includes equity at the end of a given financial year, excess equity (return on equity over cost of equity) the company is expected to generate in the estimation period and a discounted residual value post-estimation period. On one hand, the method includes profitability of the company compared to a cost of equity, but on the other hand it is strongly dependent on a number of parameters and assumptions.

The risk-adjusted net present value (rNPV) is a method used to forecast future cash flows in high-risk projects. In biotechnology, rNPV method involves forecasting future cash flows and applying probability rates of different phases of drug development. The main advantage of this method is the fact that it takes into account probability of success. The disadvantage of this method is the large number of assumptions and the high level of computational complexity.

Terminology used in the recommendation:

- P/E – price-earnings ratio
- PEG - P/E to growth ratio
- EPS - earnings per share
- P/BV – price-book value
- BV – book value
- EV/EBITDA – enterprise value to EBITDA
- EV – enterprise value (market capitalization plus net debt)
- EBITDA – earnings before interest, taxes, depreciation, and amortization
- EBIT – earnings before interest and tax
- NOPAT – net operational profit after taxation
- FCF - free cash flows
- ROE – return on equity
- WACC - weighted average cost of capital
- CAGR – cumulative average annual growth
- CPI – consumer price index
- COE – cost of equity
- L-F-L – like for like

Recommendation definitions:

- Buy - indicates a stock's total return to exceed more than 1.5x respective cost of equity over the next twelve months.
- Accumulate - indicates a stock's total return to exceed more than respective cost of equity over the next twelve months.
- Neutral - indicates a stock's total return to be in range of 0% to respective cost of equity over the next twelve months.
- Reduce - indicates a stock's total return to be in range of minus respective cost of equity to 0% over the next twelve months.

Sell - indicates a stock's total return to be less than minus respective cost of equity over the next twelve months.

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Company	Recommendation Date	Analyst	TP	Current price at the time of publication of the recommendation	Recommendation	Time horizon
Archicom	2017-04-19	Marek Szymański	22.5	16.2	Not rated	12M
Grupa Azoty	2017-04-25	Katarzyna Włodarczyk	62.1	68.9	Sell	12M
Mercator Medical	2017-04-27	Aleksandra Jakubowska	25.1	18.0	Not rated	12M
KGHM	2017-05-11	Marcin Stebakow	121	116	Neutral	12M
JSW	2017-05-11	Marcin Stebakow	112	78	Buy	12M
11 Bit Studios	2017-05-12	Jakub Rafał	255.8	177.2	Buy	12M
Warimpex	2017-05-29	Marek Szymański	5.66	5.11	Not rated	12M
Kruk	2017-06-02	Michał Fidelus	316.0	300.9	Neutral	12M
Vigo System	2017-06-12	Beata Szparaga-Waśniewska	468	372	Not rated	12M
Ciech	2017-06-13	Katarzyna Włodarczyk	72.3	65.4	Neutral	12M
Wawel	2017-06-14	Marcin Stebakow	1368.0	1175	Buy	12M
Colian	2017-06-30	Marcin Stebakow	3.48	3.50	Not rated	12M
Marvipol	2017-07-13	Marek Szymański	18.0	12.7	Not rated	12M
PKO BP	2017-07-24	Michał Fidelus	34.0	35.8	Reduce	12M
Pekao	2017-07-24	Michał Fidelus	140.0	128.0	Accumulate	12M
BZ WBK	2017-07-24	Michał Fidelus	349.0	362.5	Reduce	12M
mBank	2017-07-24	Michał Fidelus	380.0	460.0	Sell	12M
ING BSK	2017-07-24	Michał Fidelus	191.0	189.0	Neutral	12M
Handlowy	2017-07-24	Michał Fidelus	71.0	68.1	Neutral	12M
Millennium	2017-07-24	Michał Fidelus	7.1	7.5	Reduce	12M
Alior	2017-07-24	Michał Fidelus	68.0	60.5	Accumulate	12M
Getin Noble Bank	2017-07-24	Michał Fidelus	1.58	1.45	Neutral	12M
Grupa Azoty	2017-07-28	Katarzyna Włodarczyk	75.0	67.6	Accumulate	12M
JSW	2017-08-09	Marcin Stebakow	102.0	90.5	Buy	12M
Ciech	2017-08-10	Katarzyna Włodarczyk	68.0	62.5	Neutral	12M
Lotos	2017-08-21	Beata Szparaga-Waśniewska	56.0	51.0	Neutral	12M
Getback	2017-08-25	Michał Fidelus	26.6	21.8	Accumulate	12M
KGHM	2017-08-28	Marcin Stebakow	153.0	126.0	Buy	12M
Wawel	2017-08-30	Marcin Stebakow	1153	990	Buy	12M
Mercator Medical	2017-09-07	Aleksandra Jakubowska	23.1	18.0	Not rated	12M
Kruk	2017-09-14	Michał Fidelus	340.0	311.0	Accumulate	12M
Bogdanka	2017-09-21	Marcin Stebakow	95.0	78.0	Buy	12M
JSW	2017-09-28	Marcin Stebakow	107	93	Buy	12M
MZN Property	2017-10-04	Aleksandra Jakubowska	2.0	1.45	Not rated	12M
Warimpex	2017-10-11	Marek Szymański	7.3	6.73	Not rated	12M
ATC Cargo	2017-10-13	Marcin Stebakow	3.0	2.0	Not rated	12M
LPP	2017-10-19	Marek Szymański	6962.0	7960.0	Sell	12M
CCC	2017-10-19	Marek Szymański	322.0	265.3	Buy	12M
PKO BP	2017-10-24	Michał Fidelus	35.0	36.7	Reduce	12M
Pekao	2017-10-24	Michał Fidelus	139	125.2	Accumulate	12M
BZ WBK	2017-10-24	Michał Fidelus	370	356	Neutral	12M
mBank	2017-10-24	Michał Fidelus	393	452.5	Reduce	12M
ING BSK	2017-10-24	Michał Fidelus	193	191.2	Neutral	12M
Handlowy	2017-10-24	Michał Fidelus	75.0	70.0	Neutral	12M
Millennium	2017-10-24	Michał Fidelus	7.7	7.55	Neutral	12M
Alior Bank	2017-10-24	Michał Fidelus	80.0	70.2	Buy	12M
Getin Noble	2017-10-24	Michał Fidelus	1.40	1.53	Reduce	12M
Marvipol	2017-10-24	Marek Szymański	19.0	13	Not rated	12M
KGHM	2017-11-23	Marcin Stebakow	134	114.25	Buy	12M
JSW	2017-11-29	Marcin Stebakow	86.8	90.2	Reduce	12M
Vigo System	2017-12-05	Beata Szparaga-Waśniewska	455	305	Not rated	12M
LW Bogdanka	2017-12-07	Marcin Stebakow	75	95	Accumulate	12M
Śnieżka	2017-12-08	Aleksandra Jakubowska	63	69	Not rated	12M
Dom Development	2017-12-14	Marek Szymański	90	83.4	Accumulate	12M
Atal	2017-12-14	Marek Szymański	43	41.0	Neutral	12M
LC Corp	2017-12-14	Marek Szymański	3.3	2.7	Buy	12M
Robyg	2017-12-14	Marek Szymański	4.1	3.5	Accumulate	12M
Lokum Deweloper	2017-12-14	Marek Szymański	23	16.55	Buy	12M
Archicom	2017-12-14	Marek Szymański	23	15.39	Not rated	12M
PKO BP	2018-01-08	Michał Fidelus	45	44.3	Neutral	12M
Pekao	2018-01-08	Michał Fidelus	152	134.3	Buy	12M
BZ WBK	2018-01-08	Michał Fidelus	442	408.4	Accumulate	12M
mBank	2018-01-08	Michał Fidelus	443	496	Sell	12M
ING BSK	2018-01-08	Michał Fidelus	222	215	Neutral	12M
Handlowy	2018-01-08	Michał Fidelus	86	83	Neutral	12M
Millennium	2018-01-08	Michał Fidelus	8.9	9.4	Reduce	12M
Alior	2018-01-08	Michał Fidelus	87	78	Accumulate	12M
Getin Noble Bank	2018-01-08	Michał Fidelus	1.55	1.71	Reduce	12M
PKN	2018-01-09	Beata Szparaga-Waśniewska	117	106.7	Neutral	12M
Lotos	2018-01-09	Beata Szparaga-Waśniewska	54	57.4	Reduce	12M
PKP Cargo	2018-02-14	Marcin Stebakow	68	58.8	Buy	12M
BZ WBK	2018-02-21	Michał Fidelus	436	385.8	Buy	12M
Wielton	2018-02-23	Marcin Górnik	15.3	12.36	Buy	12M
Selvita	2018-03-20	Beata Szparaga-Waśniewska	85	59	Not rated	12M
JSW	2018-03-22	Marcin Stebakow	99	95.3	Neutral	12M
Marvipol Development	2018-03-26	Marek Szymański	8.9	8.7	Not rated	12M
Kruk	2018-03-28	Michał Fidelus	286	208	Buy	12M
British Automotive Holding	2018-03-28	Marek Szymański	10.5	8.3	Not rated	12M
Aplisens	2018-04-04	Michał Wojciechowski	15.1	12.9	Buy	12M
Wielton	2018-04-05	Marcin Górnik	16.0	13.7	Buy	12M
KGHM	2018-04-16	Marcin Stebakow	110.0	92.0	Buy	12M
LPP	2018-04-18	Marek Szymański	9000	8965	Neutral	12M
CCC	2018-04-18	Marek Szymański	310	272	Buy	12M