

KRUK

Birds flying high

We reiterate our **BUY** rating for Kruk (eng. raven) and significantly increase our FV to PLN 112.3 (from PLN 70) on the back of raising our estimates (2014-16E net profit up by 40%-49% (due to higher investments) and lowering the discount rate (due to decrease in interest rates in Poland). Kruk continues to deliver high double digit net profit and cash EBITDA growth driven by investments in new NPL portfolios, maintaining good recovery rates and a still low cost of funding. We think that after the purchase of a large mortgage portfolio from Getin Noble Bank this year, 2014 will be a record high in terms of investments, better than 2011 with PLN 569m. In 2014 we forecast PLN 572m purchases, which should build a decent base for future earnings and cash flows. Kruk generates an ROE of over 25%, retaining its entire profits. We assume Kruk will pay its first dividend next year, as we expect pension funds (holding ca. 52% of shares) to vote for a payment. We would see this as positive as it would help the company maintain a high ROE which we assume gradually slides to 24% by 2018E. We are ca. 20% above market consensus on 2014E-2016E EPS and believe 2Q14 results could drive a sharp upgrade in consensus.

Record net profit in 2014E boosted by non-recurrent event

We expect Kruk to post net profit of PLN 151m, positively impacted (PLN 18.7m) by the sale of receivables on real-estate collateral. On an adjusted basis (excluding one-off and portfolio revaluations) net profit would grow by 14% this year, 32% in 2015E and 16% in 2016E.

Foreign expansion seems to be closer

The company is still looking for a new foreign market to expand into. We think it needs to be done in 2-3 years to keep delivering attractive growth as the growth in current markets may not be sufficient from a long-term view. Management is still considering Spain, but we think the German market is a more likely direction for expansion - even this year. We would see such move as positive.

New share-based incentive program assumes 13% growth in EPS

The company recently also implemented a new 2015-2019 share-based incentive program that assumes 13% EPS growth each year. However given the fact that 2013 is the base for each year we see the target as undemanding. We forecast assumed growth will easily be achieved each year.

Tax is a risk

Currently Kruk uses a tax optimization structure with a Luxembourg subsidiary to lower its effective tax rate. The recent changes in legislation will make it ineffective from 2015, but Kruk says it is working on a new structure. However we cannot exclude that the new one will also become ineffective after a certain time.

Valuation offers room for upside; forecasts higher than consensus

We believe the company has an attractive growth path and this offers 17% upside potential. Kruk's 2014E P/E is 10.8x, going down to a single digit in 2015E. Kruk trades roughly in line with its foreign peers, but we think it offers more attractive exposure. We are above consensus expectations for net profit by 21%-26% for 2014-16E.



BUY

17% upside

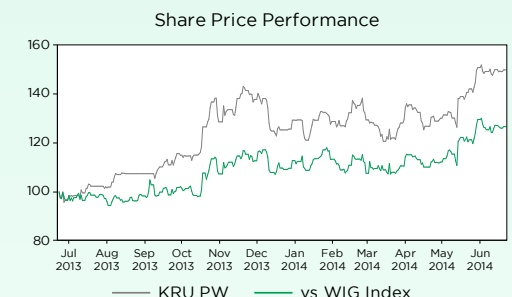
Fair Value PLN 112.30

Bloomberg ticker **KRU PW**
Share Price PLN 95.90
Market Capitalisation PLN 1,626.38m
Free Float 87%

PLN m Y/E 31-Dec	2013A	2014E	2015E	2016E
New debt portfolios purchases	368	572	522	570
Cash collections	538	634	772	951
Revenues	406	488	577	666
Cash EBITDA	349	411	508	641
EBITDA	162	219	260	298
Net Income	97.8	150.9	167.2	193.8

Y/E 31-Dec	2013A	2014E	2015E	2016E
P/E	16.6	10.8	9.7	8.4
P/BV	3.9	2.9	2.4	2.0
ROE	26.7%	30.7%	26.8%	26.0%
Dividend yield	0.0%	0.0%	3.2%	4.1%
Reported EPS (PLN)	5.7	8.8	9.8	11.2
DPS (PLN)	0.0	0.0	3.1	3.9
BV per share (PLN)	24.3	33.1	39.8	46.8

DPS based on cash flow basis



All share price data as at close on 20-Jun-2014

Source: Espírito Santo Investment Bank Research, Company Data, Bloomberg

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Summary financial information

KRUK

Rating	BUY
Fair Value (PLN)	112.3
Previous Fair Value (PLN)	70.0
change	60%
Share Price (20/06/2014, PLN)	95.9
Upside / Downside potential	17%
Bloomberg	KRU PW
Shares (m)(current)	17.0
Shares (m)(diluted)	17.6
Market Cap (PLN m)	1,626
Equity Value (PLN m)	253

Forthcoming Catalysts

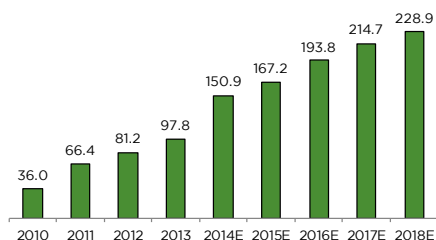
2Q14 results	01-Sep
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ES Equity Research Analyst

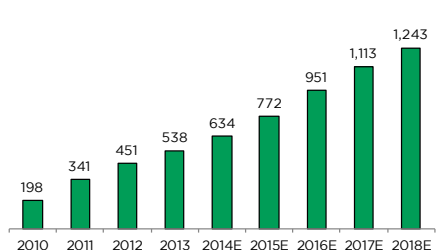
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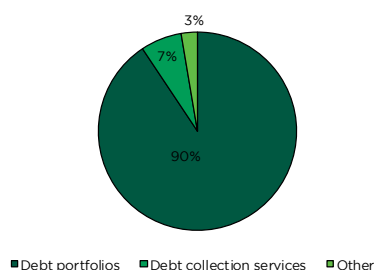
Net Profit



Cash collections



2013 Revenues split



Valuation Metrics	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
P/E	24.5	20.0	16.6	10.8	9.7	8.4	7.6	7.1
P/BV	6.8	5.1	3.9	2.9	2.4	2.0	1.8	1.6
ROE	35.9%	29.2%	26.7%	30.7%	26.8%	26.0%	24.8%	23.5%
EV / EBITDA	20.4	15.1	13.4	9.9	8.4	7.3	6.7	6.4
EV / cash EBITDA	10.3	7.5	7.1	5.9	4.8	3.8	3.2	2.8
Dividend yield	0.0%	0.0%	0.0%	0.0%	3.2%	4.1%	5.9%	7.7%

Key Ratios	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
EBITDA margin	37%	42%	40%	45%	45%	45%	44%	43%
EBIT margin	35%	40%	38%	43%	43%	43%	42%	41%
C/I	65%	61%	62%	57%	57%	57%	58%	59%
Effective tax rate	3%	5%	1%	0%	6%	6%	6%	6%
Net profit margin	24%	24%	24%	31%	29%	29%	29%	29%

Average price for purchased debt	14%	12%	11%	13%	14%	14%	14%	14%
Net Debt / EBITDA	4.3	3.8	4.0	4.0	4.0	3.8	3.6	3.4
Net Debt / Equity	1.8	1.7	1.6	1.6	1.5	1.4	1.3	1.1
Net Debt / cash EBITDA	2.1	1.9	1.9	2.1	2.0	1.8	1.5	1.3

Cash Flow Summary (PLN m)	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Cash collections	341	451	538	634	772	951	1,113	1,243
Operating expenses	(103)	(122)	(153)	(172)	(216)	(262)	(303)	(336)
Other CFO	(40)	(89)	(94)	(106)	(122)	(132)	(139)	(143)
Operating Cash Flow	198	240	291	356	434	557	670	765
New debt portfolios purchases	(569)	(309)	(368)	(572)	(522)	(570)	(600)	(609)
Other CFI	(9)	(14)	(15)	(12)	(13)	(13)	(14)	(14)
Cash Flow from Investment	(578)	(323)	(382)	(584)	(535)	(583)	(614)	(623)
Change in debt	352	121	91	225	150	95	40	(10)
Other CFF	44	(31)	(7)	0	0	0	0	0
Cash Flow from Financing	396	90	84	225	150	95	40	(10)
Cash Flow Total	16	6	(8)	(3)	50	69	96	132
cash EBITDA	212	292	344	411	508	641	761	859
YoY growth	68%	38%	18%	19%	24%	26%	19%	13%

P&L Summary (PLN m, unless stated)	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Revenues	274	343	406	488	577	666	744	801
% change	67%	25%	18%	20%	18%	16%	12%	8%
EBITDA	101	144	162	219	260	298	327	343
% change	118%	42%	13%	35%	19%	15%	9%	5%
% margin	37%	42%	40%	45%	45%	45%	44%	43%
Depreciation & Amortisation	5	7	9	11	12	13	14	14
EBIT	96	137	153	208	248	285	313	329
% change	126%	42%	12%	36%	19%	15%	9%	5%
% margin	35%	40%	38%	43%	43%	43%	42%	41%
Net Financials	(27.4)	(51.6)	(54.5)	(57.3)	(70.5)	(79.3)	(84.2)	(85.2)
Pre-Tax Profit	69	85	98	151	178	206	228	244
Income Tax Expense	2.2	3.9	0.7	0.0	10.7	12.4	13.7	14.6
Net Income	66.4	81.2	97.8	150.9	167.2	193.8	214.7	228.9
% change	85%	22%	20%	54%	11%	16%	11%	7%
EPS (PLN)	3.9	4.8	5.7	8.8	9.8	11.2	12.3	13.0
DPS (PLN)	0.00	0.00	0.00	0.00	3.09	3.91	5.61	7.39
Payout Ratio	0%	0%	0%	0%	35%	40%	50%	60%
Shares in Issue (m)	16.9	16.9	17.1	17.1	17.1	17.3	17.4	17.6

Balance Sheet (PLN m)	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Cash & Equivalents	36	43	35	32	29	31	31	34
Tangible Fixed Assets	14	17	20	21	22	22	22	22
Goodwill & Intangibles	8	8	10	10	10	10	10	10
Purchased receivables	719	873	1,064	1,443	1,717	1,945	2,110	2,203
Other Assets	24	30	33	35	36	38	40	41
Total Assets	800	971	1,163	1,542	1,815	2,047	2,213	2,311
Interest Bearing Debt	477	596	688	913	1,063	1,158	1,198	1,188
Other Liabilities	323	375	475	629	752	888	1,015	1,123
Total Liabilities	800	971	1,163	1,542	1,815	2,047	2,213	2,311
Shareholders' Equity	238	317	415	566	681	808	925	1,026
Minority Interests	0	0	0	0	0	0	0	0
Total Equity	238	318	416	566	681	808	926	1,026
Net Debt	441	554	653	881	1,034	1,127	1,167	1,154

Source: Company data, Bloomberg, Espirito Santo Investment Research for estimates

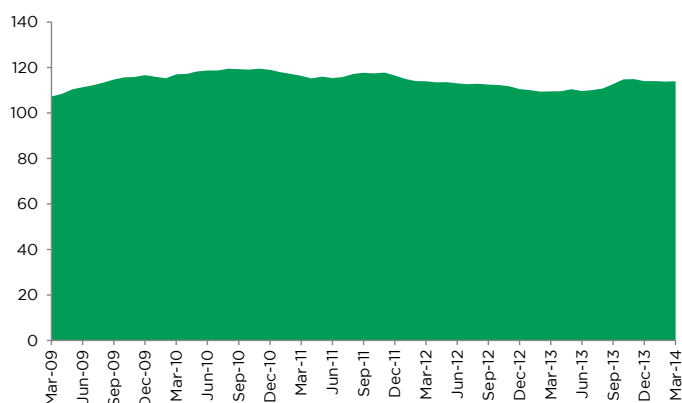


Poland – prospects for growth, but only in mid-term; mortgages may drive the market

The second half of 2013 saw a revival in consumer lending in Poland and this trend looks set to continue alongside the improving conditions in the Polish economy and growing consumer confidence. As of end 1Q14 PLN 114bn of consumer loans were granted by Polish banks, +4.1% YoY. At the same time we saw a visible improvement in the quality of these loans. The NPL ratio decreased from 17.3% in 1Q13 to 14.4% due to: 1) new production with better quality, 2) banks getting rid of old NPLs from their balance sheets; and 3) a general improvement in the economic standing of Polish households.

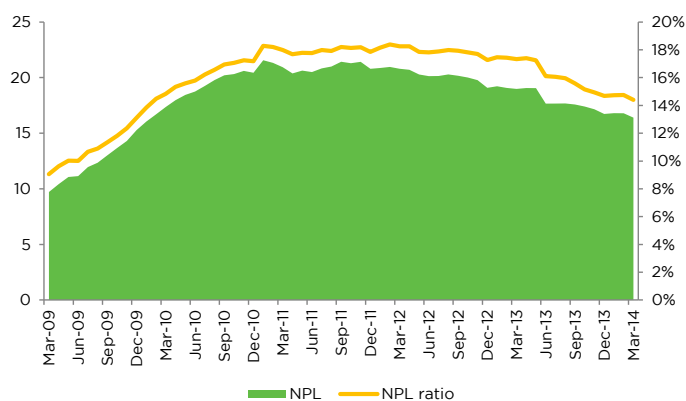
We still see some mid-term potential for Kruk to grow in Poland in consumer NPLs. We think an additional supply of bad debts may come onto the market after the banking sector assets review conducted by the National Bank of Poland. We also see a potential supply from Credit Unions (SKOKi) and non-banking lending institutions, which struggle with the weak quality of their assets, as their primary clients are those who did not meet the creditworthiness criteria at commercial banks. However we admit that we see a risk that in 3-5 years the supply of consumer NPLs in Poland could stop growing or even start slowly decreasing, putting pressure on the value of investments for local debt collectors.

Figure 1 Consumer lending in Poland (PLN bn)



Source: Espirito Santo Investment Bank Research, NBP.

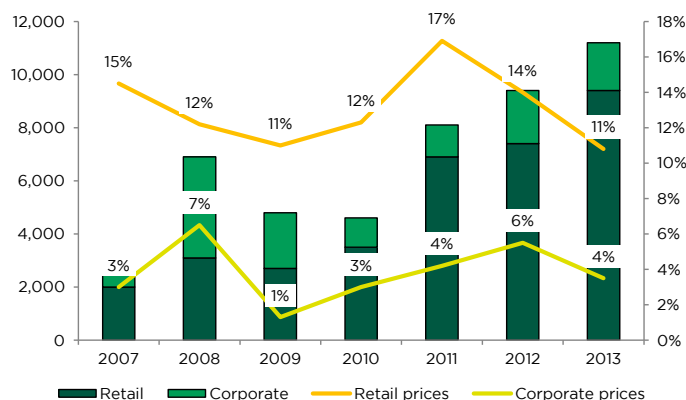
Figure 2 NPL (PLN bn) and NPL ratio in Polish banking sector



Source: Espirito Santo Investment Bank Research, NBP.

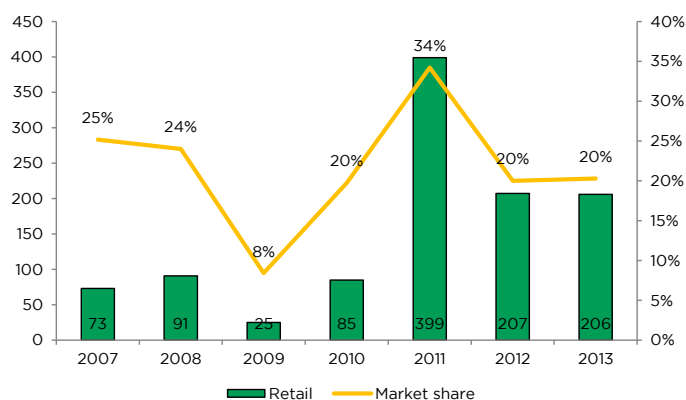
Kruk remains one of the market leaders in Poland, but competition is very strong. Last year Ultimo bought portfolios with a PLN 2.5bn nominal value vs. Kruk's PLN 2.4bn. The decrease in average prices is partially a result of lower competition than in 2011, but mostly the lower quality of debt sold by banks and other financial institutions. We expect slight pressure on prices in Poland to be visible in the coming quarters.

Figure 3 Nominal value of portfolios (PLN m) sold in Polish market



Source: Espirito Santo Investment Bank Research, Company Data

Figure 4 Kruk's retail purchases (PLN m) and market share in Poland



Source: Espirito Santo Investment Bank Research, Company Data

During several post-2013 results meetings Polish debt collectors in general appear positive about the possible supply of mortgage receivables and they think this may be a strong driver for the Polish market in the coming years. Mortgage loans had already been sold, but they were usually attached to consumer NPL portfolios or sold in very small packages. The very first big transaction took place this year. Kruk bought a mortgage portfolio with a nominal value of PLN 710m for PLN 230m from Getin Noble Bank (GNB PW, PLN 3.2, NEUTRAL, FV PLN 3.2). The portfolio consists of more than 2,000 selected mortgages (mostly Swiss franc mortgage loans converted into PLN), of which each has valid collateral (mostly flats and houses, but also plots of land). Ca. PLN 200m of nominal value is accrued penalty interest, so the effective price for the nominal loans (without interest) is ca. 45%. The company did not disclose the LtV of the acquired portfolio, but on our calculations the LtV would have to be 222% to make this transaction a pure purchase of collateral. We see this as highly unlikely.

Below we present a simple example of a theoretical borrower from an acquired portfolio, who took a mortgage loan in 2008 with a LtV of 110% when the CHF/PLN was at 2.0 (we regard this as a worst-case scenario). We assume that the Swiss franc appreciated by 70% and the value of collateral dropped by 15% (average drop in prices of flats in Poland since 2008). We also assume the borrower did not pay the capital part of instalments, so the value of outstanding debt in CHF is the same as in 2008.

Table 1 Example of theoretical borrower and LtV calculations

	2008	change	today
value of collateral (PLN)	100	-15%	85
Value of loan (PLN)	110		187
CHF/PLN	2.0	70%	3.4
CHF	55		55
LtV	110%		220%

Source: Espirito Santo Investment Bank Research, Company Data

We note that even in the worst case scenario the LtV of the theoretical borrower today does not exceed 222%. We also think that the true LtV of the acquired portfolio is much below this level, as the drop in value of collateral and/or CHF/PLN appreciation should be lower on average for the entire portfolio than assumed in our calculations. We believe this leaves upside for this investment to generate a decent return. Management also stated that it expects an IRR on this investment to be only marginally lower than for other purchases.

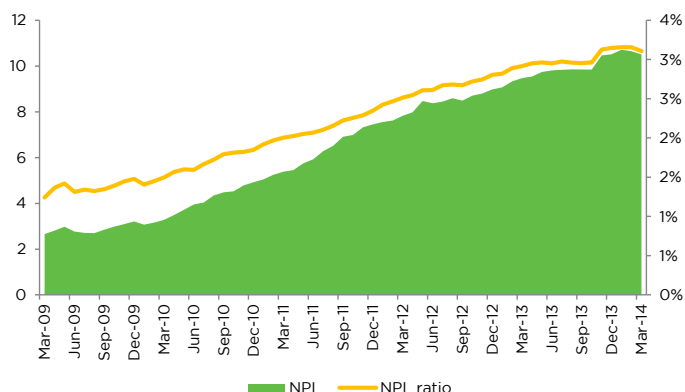
Although this transaction may be the first sign of potential mortgage NPL market growth, it is not as obvious as it seems in our opinion. Firstly the Getin portfolio was a special case. We believe the partial sale of NPLs was dictated by: 1) freeing up frozen capital; and 2) the need to clean up the portfolio and improve risk indicators before the asset review planned by National Bank of Poland.

The second important issue is related to the Polish banking sector. Currently 3.1% of mortgage loans are non-performing, which implies PLN 10.5bn of overdue nominal value and interest. According to NBP data Polish banks maintain their coverage ratio at 49%, which suggests they think they are able to recover more or less 51% of outstanding debt. Kruk paid 32.4% of nominal value (including accrued interest) for Getin's portfolio, which we see as at the upper end of the price range for mortgage portfolios which still makes the IRR on such an investment acceptable. Polish banks in general are well capitalized, have high solvency ratios and good assets quality and Poles have no major problems servicing mortgage obligations. Thus we think there is only a minor need for further provisioning of mortgage portfolios. If that is the case we could end up with a deadlock: debt collectors are unlikely to want to pay more than 35% for mortgage NPLs, while banks in general probably will not be willing to sell them at such a price as it would require the booking of additional costs of risk and lowering reported earnings. We do not rule out



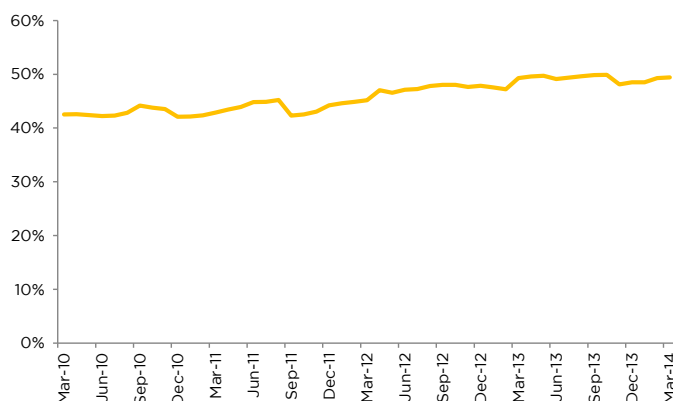
some smaller transactions taking place in the near future, but at this stage we are cautious when it comes to assuming dynamic growth in the mortgage segment and a too optimistic outlook for its evolution.

Figure 5 Polish Market - Mortgage NPL (PLN bn) and NPL ratio (%)



Source: Espirito Santo Investment Bank Research, BNP.

Figure 6 Polish market - Coverage ratio on mortgage NPL (%)

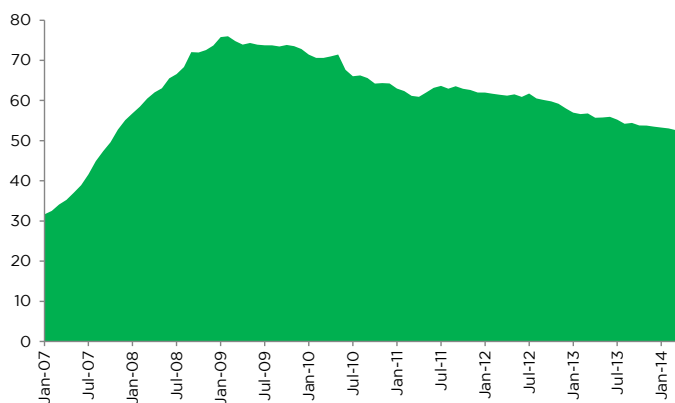


Source: Espirito Santo Investment Bank Research, BNP.

Romanian market – diverging trends

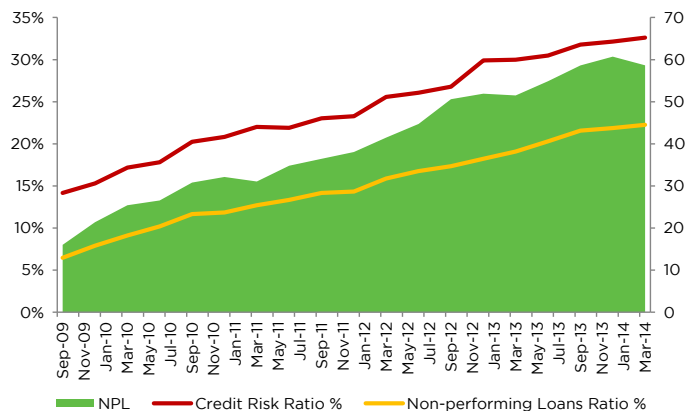
In the Romanian market we observe diverging trends in the banking sector. On the one hand consumer lending has continued to decrease since 2009. At the end of 1Q14 the value of consumer loans stood at RON 52.5bn, which translates into a 7.3% decrease YoY. On the other hand the quality of assets deteriorated further and at the end of 1Q14 the NPL ratio (based on total lending) reached 22.3% (up from 19.1% in 1Q13). On our estimates it implies ca. RON 58.6bn of overdue assets in the banking sector. We also assume that the exclusive NPL ratio for consumer lending is substantially higher than 22.3%.

Figure 7 Consumer lending in Romania (RON bn)



Source: Espirito Santo Investment Bank Research, BNP.

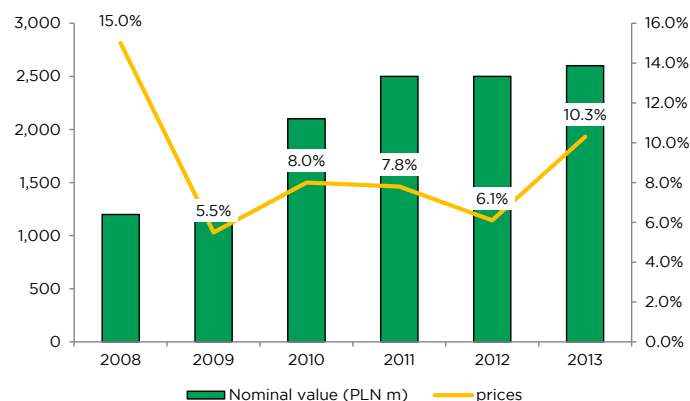
Figure 8 NPL (RON bn) and risk ratios in Romanian banking sector (%)



Source: Espirito Santo Investment Bank Research, BNP.

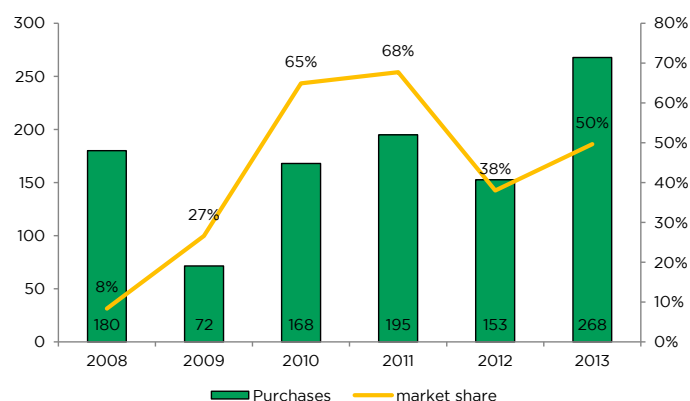
Kruk maintained its dominant position in the Romanian market with a 50% market share in 2013. We would expect Romania to continue to be an important market for Kruk, with some growth potential mostly due to unresolved problems with asset quality in the banking sector. We believe that the on-going asset quality review (AQR) conducted by the ECB may prompt some regional banks present in Romania to get rid of overdue assets faster to improve their capital position.

Figure 9 Portfolios sold (PLN m) in Romanian market



Source: Espirito Santo Investment Bank Research, Company Data

Figure 10 Kruk's purchases (PLN m) and market share in Romania



Source: Espirito Santo Investment Bank Research, Company Data

Assumptions on cash collections

After financial year 2013 Kruk presented some additional information on its historical investments in NPL portfolios and as well as the value of expected undiscounted cash collections from outstanding portfolios as of the end of 2013.

According to information presented at the end of 2013 the company had spent ca. PLN 1.8bn on non-performing receivables with a nominal value of PLN 17.9bn (estimated average price paid amounted to 9.8%). Kruk collected PLN 1.9bn until 2013 and expects ca. PLN 2.1bn in the coming years. This implies a 231% average recovery rate based on the price paid. In our model we assume Kruk collects PLN 2,097m from portfolios as of 2013 and a 230% recovery rate from portfolios bought in 2014 (except a mortgage portfolio with 218%) and onwards. One may argue that historical portfolios have higher recovery rates than those in the last 2-3 years, so this assumption may be aggressive. However we note that the company continues to increase its share of Romanian portfolios, which have better recovery rates than Polish ones, which historically constituted most of the investments. Therefore we feel pretty comfortable with this assumption.

Table 2 Assumptions on recovery rates

in PLN m	
Purchased nominal	17,917
Price paid	1,756
Price in %	9.8%
Fair value as of 2013	1,054
Cash collections	4,048
Executed up to 2013	1,943
Expected after 2013 (ERC)	2,105
Implied recovery rates	
Total as a % of nominal value	23%
Total as a % of price paid	231%
ERC as a % of fair value	200%

Source: Espirito Santo Investment Bank Research, Company Data. ERC – expected remaining collections.

To put Kruk's assumption into perspective, we note that Arrow Global (ARW LN, GBP 2.22, Not covered) assumes a 10-year ERC at 230% (as of 1Q14) for its portfolio's fair value while Intrum Justitia (IJ SS, SEK 197, Not covered) assumes ca. 210% vs 200% for Kruk. However we note that ERC depends on timing of investments: the more recent investments the higher ERC should be.

Valuation: FV up from PLN 70 to PLN 112.3

Our valuation is equally weighted between a residual income model and DCF model. Previously we used only a DCF and we feel that expansion to two methods reduces the risk to our FV, especially when they give very different indications. We also note that the results of a DCF may be skewed when a company experiences lower FCF in the early years and the bulk of the FV depends on Terminal Value calculations (as is the case with Kruk).

We use the following assumptions: risk free rate of 4.1%, equity risk premium of 5.0%, cost of equity of 11.1% for 2013-17E and 10.9% in Terminal Value (TV) and after tax cost of debt of 6.8% for 2013-17E and 5.8% in TV; we assume a long-term growth rate of 3%. We also carry out a peer multiple valuation (0% weighting) for comparison.

Table 3 DCF valuation (PLN m)

DCF Valuation	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E	TV
EBIT	42.5	96.0	136.7	152.9	208.2	248.4	285.4	312.5	328.7	338.6
tax rate	-1.4%	3.1%	2.9%	0.5%	0.0%	6.0%	6.0%	6.0%	6.0%	19.0%
tax paid	0.6	-3.0	-3.9	-0.7	0.0	-14.9	-17.1	-18.8	-19.7	-64.3
NOPAT	43.1	93.0	132.8	152.2	208.2	233.5	268.3	293.8	309.0	274.3
Depreciation	3.9	5.4	7.3	9.3	11.0	12.0	13.0	14.0	14.0	14.0
Change in WC	21.8	15.5	-28.0	0.4	2.4	7.2	7.6	7.4	6.4	6.4
Portfolios amortization	86.8	112.9	154.4	187.1	191.9	247.7	342.7	434.1	515.8	608.8
Portfolios purchases	-194.0	-568.8	-309.2	-367.5	-571.9	-521.9	-570.2	-599.7	-608.8	-608.8
CAPEX	-7.0	-9.4	-14.1	-14.7	-12.1	-12.6	-13.0	-14.0	-14.0	-14.0
FCF	-45.2	-351.5	-56.8	-33.2	-170.5	-34.1	48.4	135.5	222.4	280.6
				discount factor	0.91	0.83	0.75	0.69	0.63	
				PV FCF	-155.2	-28.2	36.5	93.1	139.1	2,755
				g	3%					
				EV	2,840					
				Net debt (as of 31.12.2013)	653					
				month	6					
				Value of equity (today)	2,309					
				PV of share-based compensation inflow	39.4					
				NOSH (m, fully diluted)	17.6					
				Fair Value (PLN)	133.5					
				upside potential	39.2%					

Source: Espirito Santo Investment Bank Research for estimates, Company Data

Table 4 Residual income model (PLN m)

Residual income model	2012	2013	2014E	2015E	2016E	2017E	2018E	TV
Net income	81.2	97.8	150.9	167.2	193.8	214.7	228.9	208.8
Equity	318	416	566	681	808	926	1,026	1,039
ROE	25.6%	26.7%	30.7%	26.8%	26.0%	24.8%	23.5%	20.2%
COE			11.1%	11.1%	11.1%	11.1%	11.1%	10.9%
excess return			96.2	97.7	110.8	118.1	120.2	93.2
PV of excess return			86.6	79.1	80.7	77.4	70.9	707.4
g			3%					
Dividend			0					
month			6					
Value of equity			1,602					
NOSH (m, fully diluted)			17.6					
Fair Value (PLN)			91.0					
upside			-5.1%					

Source: Espirito Santo Investment Bank Research for estimates, Company Data



Table 5 Peers comparisons (PLN and PLN m, prices for peers as of 23.06.2014)

Ticker	Name	Price (LCU)	FV	Rating	Mcap EUR m	P/E			P/BV			ROE			Dividend yield		
						2014E	2015E	2016E	2014E	2015E	2016E	2014E	2015E	2016E	2014E	2015E	2016E
PRAA US Equity	PORTFOLIO RECOVERY	59.0			2,184	15.0	13.0	11.2	2.8	2.3	1.9	20.8%	19.6%	18.9%	n/a	n/a	n/a
IJ SS Equity	INTRUM JUSTITIA	197.0			1,665	16.7	15.0	13.7	4.8	4.6	4.4	28.6%	31.7%	34.7%	3.3%	3.6%	3.8%
ECPG US Equity	ENCORE CAPITAL GROUP	45.0			860	10.3	8.9	7.5	1.9	1.6	1.3	16.3%	18.4%	17.6%	n/a	n/a	n/a
ARW LN Equity	ARROW GLOBAL GROUP	222.0			485	13.0	10.4	8.5	3.1	2.6	2.4	24.5%	25.5%	25.5%	2.3%	2.9%	3.7%
CCP AU Equity	CREDIT CORP GROUP LTD	9.0			279	9.8	9.8	n/a	2.2	2.0	1.8	22.5%	21.5%	21.1%	5.3%	5.1%	n/a
CLH AU Equity	COLLECTION HOUSE LTD	2.0			164	10.2	9.2	8.6	1.4	1.3	1.2	12.9%	12.8%	n/a	5.2%	n/a	n/a
median						11.7	10.1	8.6	2.5	2.2	1.9	21.7%	20.6%	21.1%	4.3%	3.6%	3.8%
KRU PW Equity	KRUK	95.9	112.3	BUY	396	10.8	9.7	8.4	2.9	2.4	2.0	30.7%	26.8%	26.0%	0.0%	3.2%	4.1%
Implied valuation (PLN m)						1,758	1,689	1,666	2,011	1,910	1,844						
Median of implied valuations (PLN m)												1,801					
Implied value per share (PLN)												102.3					

Source: Espirito Santo Investment Bank Research, for KRUK estimates, Bloomberg consensus for not rated companies

Following an increase in expected NPL investments we also raise our earnings estimates as shown below.

Table 6 Changes in forecasts

	2014			2015			2016		
	new	old	change	new	old	change	new	old	change
cash collections	634	658	-4%	772	737	5%	951	802	19%
cash EBITDA	411	440	-7%	508	497	2%	641	549	17%
net profit	151	108	40%	167	117	43%	194	130	49%

Source: Espirito Santo Investment Bank Research for estimates

We are above market consensus for this year by 24% and 26%-21% for 2015E and 2016E respectively in terms of net profit. Our revenues estimates are 3-8% above market expectations. We think that forecast excellent 2Q14 earnings may be a catalyst for consensus to upgrade.

Table 7 ESIB vs consensus (PLN m)

	2014			2015			2016		
	ESIB	cons.	diff.	ESIB	cons.	diff.	ESIB	cons.	diff.
Revenues	488	473	3%	577	538	7%	666	619	8%
net profit	151	122	24%	167	133	26%	194	161	21%

Source: Espirito Santo Investment Bank Research for estimates, Bloomberg consensus estimates

Financial statements

Table 8 P&L statements (PLN m)

P&L	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Cash collections	117.2	140.4	197.9	341.1	451.3	537.7	634.3	771.9	951.1	1112.8	1243.4
Revenues	103.9	128.6	164.3	274.1	343.0	405.6	488.2	576.7	666.4	743.6	801.4
Debt portfolios	72.5	84.7	118.1	230.4	303.0	355.7	442.5	524.1	608.4	678.7	727.7
of which: interests	63.4	78.4	99.7	210.5	298.3	369.0	436.7	524.1	608.4	678.7	727.7
revaluations	9.1	6.3	18.4	19.7	4.7	-13.2	5.7	0.0	0.0	0.0	0.0
Debt collection services	28.7	41.8	44.1	41.0	32.9	39.9	32.8	35.8	36.1	36.5	36.8
Other	2.7	2.1	2.2	2.7	7.1	9.9	12.9	16.8	21.8	28.4	36.9
Direct and indirect expenses	56.3	71.6	89.6	130.4	148.9	182.8	203.7	251.0	300.7	347.8	387.4
Debt portfolios	34.6	46.0	60.9	103.1	122.2	153.4	172.0	216.1	261.5	303.2	335.7
Debt collection services	19.4	24.0	25.8	23.3	20.5	21.2	21.3	21.5	21.7	21.9	22.1
Other	2.3	1.5	2.9	4.0	6.2	8.1	10.3	13.4	17.5	22.7	29.5
Middle margin	47.6	57.0	74.7	143.7	194.1	222.9	284.5	325.7	365.7	395.8	414.1
Debt portfolios	37.9	38.7	57.2	127.3	180.8	202.3	270.4	308.0	346.9	375.5	392.0
Debt collection services	9.2	17.7	18.2	17.7	12.4	18.7	11.5	14.3	14.4	14.6	14.7
Other	0.4	0.6	-0.7	-1.3	0.9	1.8	2.6	3.4	4.4	5.7	7.4
SG&A	19.1	21.4	28.1	40.9	50.3	60.4	65.3	65.3	67.2	69.2	71.3
EBITDA	27.4	34.8	46.5	101.4	144.0	162.3	219.2	260.4	298.4	326.5	342.7
Depreciation	2.6	3.1	3.9	5.4	7.3	9.3	11.0	12.0	13.0	14.0	14.0
EBIT	24.8	31.7	42.5	96.0	136.7	152.9	208.2	248.4	285.4	312.5	328.7
Net financial result	-8.5	-4.4	-7.0	-27.4	-51.6	-54.5	-57.3	-70.5	-79.3	-84.2	-85.2
Gross profit	16.3	27.3	35.5	68.6	85.1	98.5	150.9	177.9	206.1	228.4	243.5
Tax	-0.4	3.8	-0.5	2.2	3.9	0.7	0.0	10.7	12.4	13.7	14.6
Net profit	16.7	23.5	36.0	66.4	81.2	97.8	150.9	167.2	193.8	214.7	228.9
Adjusted net profit	7.6	17.2	17.6	46.7	76.5	111.0	145.2	167.2	193.8	214.7	228.9
* Adjusted net profit = Net profit - revaluations recognized in P&L											
cash EBITDA	72.1	90.5	126.3	212.2	292.3	344.3	411.1	508.1	641.1	760.6	858.5
Key ratios	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Interests / cash collections	54%	56%	50%	62%	66%	69%	69%	68%	64%	61%	59%
Expenses / cash collections	29%	33%	31%	30%	27%	29%	27%	28%	28%	27%	27%
Debt collection services margin	32%	42%	41%	43%	38%	47%	35%	40%	40%	40%	40%
cash EBITDA margin	49%	49%	52%	55%	60%	59%	60%	62%	64%	65%	65%
Net profit margin	16%	18%	22%	24%	24%	24%	31%	29%	29%	29%	29%
C/I	76%	75%	74%	65%	61%	62%	57%	57%	57%	58%	59%
Effective tax rate	-2.5%	14.1%	-1.4%	3.1%	4.6%	0.7%	0.0%	6.0%	6.0%	6.0%	6.0%
Dynamics YoY	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Cash collections		20%	41%	72%	32%	19%	18%	22%	23%	17%	12%
Revenues		24%	28%	67%	25%	18%	20%	18%	16%	12%	8%
cash EBITDA		25%	40%	68%	38%	18%	19%	24%	26%	19%	13%
Net profit		41%	53%	85%	22%	20%	54%	11%	16%	11%	7%
Adj net profit		127%	2%	165%	64%	45%	31%	15%	16%	11%	7%
Other figures	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
NPL portfolios	152	155	263	719	873	1,054	1,434	1,708	1,936	2,101	2,194
Net debt	82	39	101	441	554	653	881	1,034	1,127	1,167	1,154
Total assets	212	208	318	800	971	1,163	1,542	1,815	2,047	2,213	2,311
Equity	77	100	132	238	318	416	566	681	808	926	1,026
ROA	8%	11%	14%	12%	9%	9%	11%	10%	10%	10%	10%
Asset / Equity	2.8	2.1	2.4	3.4	3.1	2.8	2.7	2.7	2.5	2.4	2.3
ROE	22%	27%	31%	36%	29%	27%	31%	27%	26%	25%	23%
Net debt / Equity	1.1	0.4	0.8	1.8	1.7	1.6	1.6	1.5	1.4	1.3	1.1
Net debt / cash EBITDA	1.1	0.4	0.8	2.1	1.9	1.9	2.1	2.0	1.8	1.5	1.3

Source: Espirito Santo Investment Bank Research for estimates, Company Data. * Net profit adj = Net profit - revaluations.



Table 9 Balance sheet statement (PLN m)

Balance sheet	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Fixed assets	21	15	19	24	27	34	35	36	36	36	36
Tangible fixed assets	8	8	10	14	17	20	21	22	22	22	22
Intangible assets	3	4	6	8	8	10	10	10	10	10	10
Other	10	3	3	2	3	3	3	3	3	3	3
Current Assets	191	193	299	777	944	1,129	1,507	1,780	2,011	2,178	2,275
Inventories	1	1	0	1	1	1	1	1	1	1	1
Receivables	8	10	11	13	12	9	10	12	13	15	16
Investments in NPL portfolios	152	155	263	719	873	1,064	1,443	1,717	1,945	2,110	2,203
Cash and equivalents	25	24	21	36	43	35	32	29	31	31	34
Other	5	3	4	8	15	20	21	21	21	21	21
TOTAL ASSETS	212	208	318	800	971	1,163	1,542	1,815	2,047	2,213	2,311
Long-term liabilities	56	22	78	339	409	513	738	888	983	1,023	1,013
financial	56	14	78	339	409	513	738	888	983	1,023	1,013
non-financial	0	8	0	0	0	0	0	0	0	0	0
Short-term liabilities	79	86	108	223	245	234	237	246	255	264	272
financial	51	49	44	138	187	175	175	175	175	175	175
payables	19	27	49	67	39	36	39	48	57	66	74
other	9	11	14	18	19	24	24	24	24	24	24
Equity	77	100	132	238	318	416	566	681	808	926	1,026
Equity Capital	28	28	24	106	104	104	104	104	104	104	104
Retained earnings	49	72	108	132	214	311	462	576	703	821	921
Minorities	0	0	0	0	0	0	0	0	0	0	0
TOTAL LIABILITIES	212	208	318	800	971	1,163	1,542	1,815	2,047	2,213	2,311

Key figures	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
Debt	107	63	122	477	596	688	913	1,063	1,158	1,198	1,188
Net debt	82	39	101	441	554	653	881	1,034	1,127	1,167	1,154
Net debt / equity	1.1	0.4	0.8	1.8	1.7	1.6	1.6	1.5	1.4	1.3	1.1
Assets / Equity	2.8	2.1	2.4	3.4	3.1	2.8	2.7	2.7	2.5	2.4	2.3

Source: Espirito Santo Investment Bank Research for estimates, Company Data

Table 10 Cash flow statement (PLN m)

Cash flow	2008	2009	2010	2011	2012	2013	2014E	2015E	2016E	2017E	2018E
CFO	89	108	124	198	240	291	356	434	557	670	765
Cash collections	117	140	198	341	451	538	634	772	951	1,113	1,243
Operating expenses	-35	-46	-61	-103	-122	-153	-172	-216	-262	-303	-336
Debt collecting services margin	9	18	18	18	12	19	11	14	14	15	15
SG&A	-19	-21	-28	-41	-50	-60	-65	-65	-67	-69	-71
Interest expenses, tax and others	16	17	-3	-17	-51	-52	-52	-71	-80	-85	-86
CFI	-106	-58	-201	-578	-323	-382	-584	-535	-583	-614	-623
New debt portfolios purchases	-104	-54	-194	-569	-309	-368	-572	-522	-570	-600	-609
Other CAPEX	-3	-4	-7	-9	-14	-15	-12	-13	-13	-14	-14
CFF	32	-52	74	396	90	84	225	97	28	-57	-139
Debt and leasing	75	7	17	195	374	618	315	30	0	0	0
Bonds	0	0	112	291	190	250	160	120	95	40	-10
Debt and leasing repayments	-46	-48	-38	-104	-323	-675	-200	0	0	0	0
Bond repayments	0	0	-34	-30	-120	-102	-50	0	0	0	0
Dividend	0	0	0	0	0	0	0	-53	-67	-97	-129
Other	3	-11	17	44	-31	-7	0	0	0	0	0
Cash at the beginning of the period	11	25	24	21	36	43	35	32	29	31	31
Cash at the end of the period	25	24	21	36	43	35	32	29	31	31	34

Source: Espirito Santo Investment Bank Research for estimates, Company Data

Valuation Methodology

Our valuation is based on a DCF model and residual income model with equal weighting. We use with the following assumptions: risk free rate of 4.1%, equity risk premium of 5.0%, cost of equity of 11.1% for 2013-17E and 10.9% in Terminal Value (TV) and after tax cost of debt of 6.8% for 2013-17E and 5.8% in TV; we assume a long-term growth rate of 3%. We also carry out a peer multiple valuation (0% weighting) for comparison.

Risks to Fair Value

Downside risk to overall macroeconomic conditions, especially households' financial standing due to higher unemployment rate, slower GDP growth or lower wages;

Growing competition – pressure on receivables' prices. The competition for receivables in Poland is strong and growing, which might put further pressure on NPL prices and ultimately decrease margins;

FX rate movements: mainly appreciation PLN against RON impacting debt portfolios' fair value and equity capital

Tax legislation which may cause current and future tax optimization structures to be ineffective.



Please visit our website at www.EspiritoSantoIB.co.uk for up to date recommendation charts.



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BUY	Analyst expects at least 10% upside potential to fair value, which should be realized in the next 12 months
NEUTRAL	Analyst expects upside/downside potential of between +10% and -10% to fair value, which should be realized in the next 12 months
SELL	Analyst expects at least 10% downside potential to fair value, which should be realized in the next 12 months
TRADING RATING	DEFINITION
TRADING BUY	Analyst expects a positive short-term movement in the share price (max duration 3 months from the time Trading Buy is announced) and may move out of line with the fair value estimate during that period
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Buy	199	46.1%	26	81.3%	6.0%
Neutral	135	31.3%	4	12.5%	0.9%
Sell	97	22.5%	2	6.3%	0.5%
Restricted	0	0.0%	0	0.0%	0.0%
Under Review	1	0.2%	0	0.0%	0.0%
Trading Rating:					
Trading Buy	0	0.0%	0	0.0%	0.0%
Trading Sell	0	0.0%	0	0.0%	0.0%
Total recommendations	432	100%	32	100%	7.4%

For further information on Rating System please see "Definitions and distribution of ratings" on: <http://www.espiritosantoib-research.com>.

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