



Bank Saint-Petersburg

Company
Note

HOLD

Upside: 4%

Target Price: \$4.50

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Stock data

Ticker	STBK, STBKP	M.Cap, \$ mn	1,007
Shares Ords (ex IPO)	231,400,000	Free Float, %	
Shares Ords (Post IPO)	282,200,000		
Shares Prefs	20,100,000	Free Float, \$ mn	
Bid Ords, \$	4.35	Offer Ords, \$	5.00
Bid Prefs, \$	1.00	Offer Prefs, \$	1.30

Financials, 2007E

Assets, \$ mn	4,023	ROE	19.0
Book Value, \$ mn	617	P/E	13.4
Net income, \$ mn	75	P/BV	2.4

Litmus test for a renewed wave of IPOs in the banking sector

- Bank Saint-Petersburg (BSPb) is the first private Russian bank, which has decided to conduct an IPO and has announced the price band within which it will issue new shares. Given the difficult situation on global financial markets, which has negatively affected financial sector valuations, the results of the IPO may encourage other banks – that had postponed their IPOs due to the problems prevalent in financial markets – to follow BSPb's example.

- The bank has a strong position in the regional market (being ranked 3rd or 4th) and is amongst the Top-30 Russian banks. Its asset growth rate (CAGR 78%) and net profit growth rate (CAGR above 100%) have outperformed the average market indicators over the past few years, with a high ROE rate of over 30% in 2006.

- Although the bank presents itself as the only independent bank in St. Petersburg and states that there are no significant governmental, financial or industrial special interest groups supporting it, in our opinion, the shareholder structure implicitly points to relatively close business relations between the bank's owners and management and the municipal administration. We consider this to be a competitive advantage of the bank, at least, in the short term.

- Raising additional equity and debt capital would enable the bank to maintain its high growth rates over the next few years, diversify its funding base, and reduce its liquidity deficit. We expect the issuance of GDRs (even without listing) to result in greater transparency.

- The announced IPO price band of \$4.35-5.65 per share implies P/E-2007F levels of 13.4-17.4 (excluding the IPO) and 16.4-21.2 (including the IPO) and P/BV-2007F ranging from 2.4-3.1 (before the IPO) and 2.0-2.6 (after the IPO). We believe that below the declared mid-range IPO price, the bank's financial indicators will be more attractive than the average market indicators. However, in our opinion, the bank is exposed to additional risks due to its relatively small size, its regional status, its low share liquidity, the concentration of its equity capital amongst a limited number of principal shareholders and the risks that could arise from changes in their composition, and a lack of transparency. Some of these disadvantages might be eliminated after the IPO, which could lead to an increase in the bank's share price.

- **We estimate the bank's year-end fair value (assuming the IPO takes place) at \$1.29 bn. Accordingly, we initiate coverage of the bank by issuing a HOLD recommendation with a target price of \$4.5 per ordinary share, which gives potential upside of 4% from the current price.** We would recommend investors to participate in the IPO if the price offered is close to the lower end of the bank's indicated price range.



Information on the IPO

On October 9, 2007 Bank Saint-Petersburg announced its intention to conduct an IPO of its ordinary shares as well as a GDR issue before the end of the year. The bank will issue 50.8 mn ordinary shares (amounting to 18% of the total number of the bank's ordinary voting shares after the IPO). Recently, the bank had listed its ordinary shares on both the RTS and MICEX stock exchanges. The projected IPO will be conducted both in Russia and abroad (excluding the USA), and the GDRs will be placed without listing. Deutsche Bank and Renaissance Capital will arrange the IPO. On October 19, the Federal Financial Markets Service (FFMS) approved BSPb's IPO, allowing up to 70% (corresponding to 11.7% of the increased charter capital) of the shares to be issued abroad.

On October 23, the bank announced its indicative price band for the IPO ranging between \$4.35-5.65 per share and \$13.05-16.95 per GDR. The announcement of the IPO's indicative price range boosted the bank's share price from \$3.33/4.29 per share on October 22, to \$4.35/5.00 per share on the following day, when shares were traded at \$4.29 for the first time over the last 10 days. On October 24, the bank's share price reached the lower end of the indicated IPO price band.

	Lower band	Higher band	Mid-range	SOVLINK Target price estimate	Market price on 24.10.2007
Price, \$ per share	4.35	5.65	5.00	4.50	4.35
Upside to current market price, %	0.0%	29.9%	14.9%	3.5%	-
Bank's capitalisation before the IPO, \$ mn	1,007	1,307	1,157	1,041	1,007
Value of offered block (50.8 mn shares), \$ mn	221	287	254	229	221
Bank's capitalisation after the IPO, \$ mn	1,227	1,594	1,411	1,270	1,227
P/BV-1H07	3.5	4.5	4.0	3.6	3.4
P/BV-2007F (w/o IPO)	2.4	3.1	2.8	2.5	2.4
P/BV-2007F (with IPO)	2.0	2.6	2.3	2.1	2.0
P/E-2007F (with IPO)	16.4	21.2	18.8	16.9	16.4

Source – Company data, RTS Board, SOVLINK estimates

At the moment the bank's shares are traded on the RTS Board. The Bank has completed its listing procedure for the RTS and MICEX, and is expected to start trading on these exchanges after its IPO. We expect the issuance of new shares, amounting to 18% of the increased capital, to boost the liquidity of the bank's shares, which is quite low at the moment. The bank needs to improve its transparency as well as the accessibility of documents, including its actual IFRS accounts. Whilst the IPOs on both Russian and foreign markets could improve transparency considerably (as the bank will be obliged to release quarterly reports under IFRS, create an IR department, hold regular meetings with investors and conference calls, etc.) – nonetheless, the bank will be able to avoid the more stringent requirements required for IPO issues of ordinary shares abroad, since GDRs are not required to undergo listing procedures.



SWOT – analysis

Strengths	Weaknesses
<p>The Bank ranks 3rd or 4th in the Saint-Petersburg regional banking sector and is one of the Top-30 Russian banks, with a Ba3 credit rating from Moody's and a B rating by Fitch.</p> <p>Asset growth rates are significantly higher than average industry indicators given high returns (ROE exceeded 30% in 2006).</p> <p>Large client base, low dependence on foreign borrowings (deposits account for about 80% of its liabilities)</p> <p>Low credit risks (proportion of overdue loans is below average industrial indicators and is covered 10 times by provisions).</p> <p>Good relationships with the municipal authorities.</p> <p>Great opportunities for distributing its banking products through a well diversified network of city branches and ATMs, the use of an Internet-banking system, and cross sales).</p>	<p>Regional status of the bank, limited of resources</p> <p>Deficit of long-term financial resources to develop its credit portfolio (in 2006, about 89% of its liabilities had maturities of less than one year).</p> <p>Relatively high concentration of major borrowers (39% of its loan portfolio) and key accounts (23.5% of total customer accounts).</p> <p>Minor share of retail loans limits its potential to maintain high interest margins.</p> <p>Relatively low transparency level</p>
Opportunities	Threats
<p>Prospects for consolidation of regional markets on the base of banks which have strong positions in the region – including the issuer.</p> <p>Raising additional shareholders' equity and loan capital will allow the bank to maintain its high growth rates in the near future, to diversify risks due to a highly concentrated funding base and reduce its liquidity deficit.</p> <p>Opportunities to participate in projects supported by the Saint-Petersburg authorities.</p> <p>Expansion of its branch network, branches in Moscow and plans to open branches in other Russian regions will allow the bank to expand its business – at the same time, the bank is not planning to expand aggressively beyond its local region.</p>	<p>Stronger regional competition with leading state banks (Sberbank, VTB) and branches of the largest private banks.</p> <p>Aggressive expansion of subsidiaries of foreign banks in the North-Western region.</p> <p>Stricter terms for raising funds in loan markets, stronger competition for retail and corporate deposits.</p> <p>Lower interest margins and ROE.</p>



Table 3 – Projected income statement, \$ mn

	2005	2006	2007E	2008E	2009E	2010E
Interest income on loans	93	161	314	471	607	740
Interest expenses	-33	-61	-147	-228	-297	-365
Net interest income	60	100	166	243	310	375
Provisions for loan impairment	-17	-18	-35	-33	-34	-37
Net interest income after provision for loan impairment	43	82	132	209	276	338
Net fee and commission income	14	21	31	44	60	76
Operating income	68	114	181	281	373	461
Operating costs	-40	-56	-82	-126	-171	-214
Profit before tax	28	58	99	155	202	247
Profit tax	-6	-14	-24	-37	-49	-59
Net profit	22	44	75	118	154	188

Source: Company data, SOVLINK forecast

Table 4 – Projected balance sheet, \$ mn

	2005	2006	2007E	2008E	2009E	2010E
Cash and cash equivalents	158	333	402	482	587	673
Mandatory reserves	17	29	56	75	97	121
Securities	116	283	402	535	690	863
Loans to other banks	73	70	121	161	207	259
Loans and advances to customers	662	1,508	2,896	3,906	5,107	6,470
Fixed assets	48	61	121	144	173	198
Other assets	7	16	24	48	41	43
Total assets	1,082	2,301	4,023	5,350	6,902	8,627
Bank credits and deposits	45	29	38	55	60	76
Customer deposits	814	1,700	2,758	3,602	4,666	5,787
Own debt securities	98	267	347	508	722	983
Other borrowings	1	124	228	416	542	681
Other liabilities	8	10	34	37	30	38
Total liabilities	967	2,130	3,405	4,618	6,021	7,564
Total shareholders' equity	115	171	617	732	881	1063

Source: Company data, SOVLINK estimates

Table 5 – Financial ratios

	2005	2006	2007E	2008E	2009E	2010E
P/E	46.2	23.4	16.6	10.6	8.1	6.7
P/BV	8.9	6.0	2.0	1.7	1.4	1.2
ROE	24.3%	30.6%	19.0%	17.5%	19.1%	19.3%
ROA	2.6%	2.6%	2.4%	2.5%	2.5%	2.4%
Cost/Income	47%	43%	38%	40%	42%	43%
Fees & commission / operating income	20%	19%	17%	16%	16%	17%
Net interest income (after loan impairment provisions) / operating income	63%	72%	73%	74%	74%	73%
Provisions / Loans	5.8%	3.9%	3.2%	3.2%	3.1%	3.0%
Earning asset yield	13.9%	11.8%	11.9%	11.7%	11.5%	10.9%
Cost of liabilities	-4.7%	-3.9%	-5.4%	-5.7%	-5.6%	-5.4%
Net interest spread	9.2%	7.9%	6.5%	6.0%	5.8%	5.5%
Net interest margin	8.9%	7.4%	6.3%	6.1%	5.9%	5.5%

Source: Company data, SOVLINK estimates



Valuation of ordinary shares

We estimate the bank's fair value based on the modified Gordon growth model (Target P/BV), where $(P/BV = (ROE - g) / (r - g))$. We assume a terminal ROE rate of 19%, and a discount rate of 13.34%.

Risk-free rate in Russia	5.75%	Russian-30 YTM
Risk premium for investments on the US stock market	4.36%	Historical for the period from 1929 to 2005
Sovereign risk premium for Russian equity	1.65%	Based on Russia's sovereign credit rating and adjustments for excessive risk of investments in shares as opposed to Eurobonds
Russian equity risk premium	6.0%	
Beta	0.93	
Risk premium for investment in the company	5.59%	
Liquidity premium	1.50%	
Transparency & Disclosure premium	0.5%	
Cost of equity	13.34%	

	2006	2007E	2008E	2009E	2010E
Shareholders' equity, \$ mn	171	617	732	881	1,063
Net profit	44	75	118	154	188
Equity value			13.34%	13.34%	13.34%

Applying the Gordon model we obtain a target P/BV-2010F of 1.77. Taking the forecast BV-2010 equal of \$1,063 mn, we obtain the bank's fair value at the end of 2010 to be $P-2010 = \$1,882.9$ mn.

Having discounted the value as at the end of 2007, we obtain $P-2007 = \$1,293.2$ mn, with a target price of \$4.5 per share at the end of 2007.

Terminal ROE rate	19.0%
Terminal growth rate	6.0%
Target P/BV-2010	1.77
Fair value of equity (P-2010), \$ mn.	1,882.9
Discount rate	13.34%
Fair value of equity at the end of 2007, \$ mn	1,293.2
Ordinary shares after SPO, mn.	282.2
Preferred shares, mn.	20.1
Total shares (adjusted)	287.35
Fair value of 1 ordinary share, \$	4.50
Fair value of 1 ordinary share at the end of 2007, \$	4.50
Market value of 1 ordinary share (24.10.2007)	4.35
Upside, %	3.5%
Recommendation	HOLD

Accordingly, we initiate coverage of the bank by issuing a **HOLD** recommendation with a target price of **\$4.5 per ordinary share, which gives potential upside of 4% from the current price**. We would recommend investors to participate in the IPO if the price offered is at the lower end of the bank's indicated price range.



Peer comparison

Bank	Ticker	Country	M.Cap, \$ mn	ROE, %		P/E			P/BV		
				2006E	2007E	2006E	2007E	2008E	2006E	2007E	2008E
Sberbank	SBER	Russia	96,333	31%	23%	31.62	22.62	16.93	8.22	3.82	3.13
Bank of Moscow	mmbm	Russia	6,500	20%	19%	31.42	21.78	15.51	5.35	3.64	3.06
Vozrozhdenie	VZRZ	Russia	1,318	19%	20%	44.73	21.54	14.20	6.30	2.90	2.53
Rosbank	ROSB	Russia	4,967	12%	15%	35.48	25.42	19.87	4.66	3.21	2.78
VTB	VTBR	Russia	32,276	19%	11%	27.38	27.35	17.16	4.62	2.05	1.85
Ursa bank	URSAP		2,268	16%	19%	42.10	18.90	9.27	2.32	2.05	1.69
Average				20%	18%	34.12	23.74	16.73	5.83	3.12	2.67

Source – Bloomberg, Company data, SOVLINK estimates

A comparison with market peers shows that even assuming a price of \$5 per share, which corresponds to the mid-range of the indicative IPO price band, the bank's shares trade at a discount to average market indicators. We consider that this is due to the relatively small size of the bank, its regional status, its low share liquidity level, and its (currently) low transparency level. In our opinion, Vozrozhdenie and Ursa-bank, a large regional bank, are its closest market peers.

Conclusions

1. Bank Saint-Petersburg is the first private Russian bank, which has decided to conduct an IPO and has announced the price band within which it will issue new shares. Given the difficult situation on global financial markets, which has negatively affected financial sector valuations, the results of the IPO may encourage other banks – that had postponed their IPOs due to the problems prevalent in financial markets – to follow BSPb's example.
2. The bank has a strong position in the regional market (being ranked 3rd or 4th) and is amongst the Top-30 Russian banks. Its asset growth rate (CAGR 78%) and net profit growth rate (CAGR above 100%) have outperformed the average market indicators over the past few years, with a high ROE rate of over 30% in 2006.
3. Although the bank presents itself as the only independent bank in St. Petersburg and states that there are no significant governmental, financial or industrial special interest groups supporting it, in our opinion, the shareholder structure implicitly points to relatively close business relations between the bank's owners and management and the municipal administration. We consider this to be a competitive advantage of the bank, at least, in the short term.
4. The bank's strength lies in its large corporate client base, low dependence on foreign debts (about 80% of its liabilities is derived from customer accounts), which allows the bank to raise relatively cheap capital. However, 90% of its liabilities are short-term deposits (with maturities of less than one year). Thus, the bank suffers from a deficit of long-term resources to develop its credit portfolio. Other risks include the high concentration of major borrowers in its loan and deposit portfolios.
5. Raising additional equity and debt capital would enable the bank to maintain its high growth rates over the next few years, diversify its funding base, and reduce its liquidity deficit. We expect the issuance of GDRs (even without listing) to result in greater transparency.
6. In our opinion, the major risk factors for the bank include tougher competition in the banking sector in the North-Western region (with its main competitors being the largest state banks, such as Sberbank and VTB, and subsidiaries of foreign banks), more stringent requirements to raise debt capital, and increased competition for corporate and retail deposits. All these factors are expected to result in a decline of the bank's interest margins and ROE rate.
7. The announced IPO price band of \$4.35-5.65 per share implies P/E-2007F levels of 13.4-17.4 (excluding the IPO) and 16.4-21.2 (including the IPO) and P/BV-2007F ranging from 2.4-3.1 (before the IPO) and 2.0-2.6 (after the IPO). We believe that below the declared mid-range IPO price, the bank's financial indicators will be more



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October 29, 2007

attractive than the average market indicators. However, in our opinion, the bank is exposed to additional risks due to its relatively small size, the regional status of the bank, its low share liquidity, the concentration of its equity capital amongst a limited number of principal shareholders and the risks that could arise from changes in their composition, and a lack of transparency. Some of these disadvantages might be eliminated after the IPO, which could lead to an increase in the bank's share price.

8. **We estimate the bank's year-end fair value (assuming the IPO takes place) at \$1.29 bn. Accordingly, we initiate coverage of the bank by issuing a HOLD recommendation with a target price of \$4.5 per ordinary share, which gives potential upside of 4% from the current price. We would recommend investors to participate in the IPO if the price offered is close to the lower end of the bank's indicated price range.**



STOCK RATING POLICY

STRONG BUY:	Upside over 25%; confidence level – high / upside over 100%; confidence level - low
BUY:	Upside between 15 and 25%; confidence level – high / upside between 25% and 100%; confidence level – low
HOLD:	Upside of less than 15%; confidence level – high / upside of less than 25%; confidence level – low
SELL:	Fair value at or below current price levels

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