

Belenkaya Olga, macro&financial sector analyst,
belenkayao@sovlink.ru

Sberbank – TP revision

BUY

Target price: US\$ 3.77
Upside: 47%

Stock data

Ticker	SBER	M.Cap \$ mn	55478
Shares Ords'000	21586948	Free Float, %	40
Shares Pref '000	1000000	Free Float, \$ mn	22191
Bid Ords, \$	2.55	Offer Ords, \$	2.62

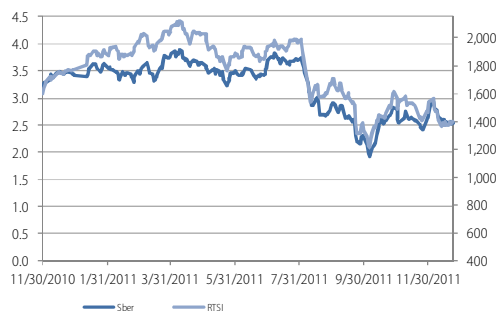
Market performance

		1 month	6 months
Absolute	Ords	-0.4%	-30.7%
Relative to RTSI	Ords	4.8%	-1.4%
Price range, \$			
High	Ords	2.92	3.74
Low	Ords	2.41	1.92

Financials, 2011E

Assets, \$ mn	316,379	P/E	5.2
Book value, \$ mn	39,750	P/BV	1.4
Net income, \$ mn	10,662	ROE	27.9%

Relative performance



Source: RTS

- We updated the target price for Sberbank, taking into consideration 9M11 IFRS results and management outlook from the conference call and the analyst meeting. We also prolonged the model horizon to the end of 2014 and lowered terminal growth rate from 6% to 5%.

- One of the positive factors for bank valuation is higher loan growth forecast. Management expects aggressive growth of the loan book in 2012 (24-25%). We think this forecast is too optimistic but nevertheless we raise loan book growth forecast for FY11-12. In 2011 we now expect loan book growth by 29%, in 2012 – some cooling of the growth to 19%.

- Net interest margin (NIM) in 3Q peaked due to the lag effect from lowering cost of retail deposits and increasing the share of high-yielding assets. In 4Q and 2012 we expect NIM to weaken due to rising cost of funding and the pressure of low lending rates for large corporate borrowers. We expect NIM to be around 6.5% in 2011, 6.3-6.4% - in 2012-2014 – best among Russian public banks.

- The bank's management estimates CoR in 12FY in the baseline scenario close to 11FY level (about zero). In the stress scenario management's "conservative" estimate of CoR is "no more than 1%" – we remind that in 09FY it was about 7%. We consider this view as too optimistic too (some metal&mining companies are already negotiating on debt covenants easing) and apply CoR forecast in the baseline scenario at 1.2% in 2012 and at 1.3-1.5% - for next 2 years.

- The bank's CFO A. Karamzin said that the operating costs growth will diminish from around 30% in 2011 to "low teens" in 2012. We cut our costs outlook for FY12 from 16% to 13%, expect low two-digit growth in the following 2 years.

- We raised our net income outlook for 2011 by 8% (to 312 bln Rub), for 2012 - by 5% (to 272 bln Rub), for 2013 - by 4% (to 305 bln Rub.). Only in 2014 we expect the net income to exceed the estimated 11FY record. The management's forecast is much more optimistic – they expect in the FY12 in the baseline scenario net income more than in FY11 (300-310 bln Rub)

- After the model revision, we increase 12-month target price of Sberbank ordinary shares from \$ 3.45 to **\$3.77** per share, reiterate the recommendation "**BUY**". For preferred shares we raise the TP from \$2.57 to **\$2.83** per share, recommendation "**BUY**".

- Market ratios for Sberbank (P/E 12E 6.6, P/BV 12E 1.2) look attractive compared to global peers (average EM P/E 12E = 7.2, P/BV 12E = 1.0). even according to our conservative outlook. Market consensus for Sberbank is P/E12 5.9, P/BV12 1.2. Sberbank now is trading with a premium to other Russian banks, for which MCap fell below 1.0 BV – nevertheless we think the premium is justified by the large capital adequacy ratio, favorable terms of access to liquidity, the stable funding base and the cheapest in Russia cost of funding. The key risk is Russian macro conditions deterioration. Among the potential drivers we see the possible privatization of CBR stake after presidential elections in March 2012.

We updated the target price for Sberbank (Sber), taking into consideration 9M11 IFRS results and management outlook from the conference call and the analyst meeting. We also prolonged the model horizon to the end of 2014.

Key changes in the model

1. Macro outlook

Macro indicators, bln Rub	2008	2009	2010	2011F	2012F	2013F	2014F
Oil price, Urals, \$/barr	94	61	78	107	87	92	99
GDP	41,668	38,76	44,939	53,382	59,864	67,084	74,654
growth rate, %	5.6%	-7.9%	4.0%	4.2%	3.5%	4.0%	4.2%
CPI	13.3%	8.8%	8.8%	6.7%	7.2%	6.8%	6.2%
Exchange rate Rub/USD EOP	29.38	30.24	30.48	31.50	32.80	31.60	30.20
Exchange rate Rub/USD average annual	24.81	31.68	30.31	29.28	32.15	32.20	30.90

() – previous forecast

2. Loan book

Strong loans growth in 3Q resulted in 18.1% YTD loan book increase which exceeds our FY11 forecast (18%). In October-November the loan growth accelerated and achieved 26,6% YTD (RAS). Therefore we raise FY11 loan growth forecast to 29%.

In FY12 Sberbank management expects the loan growth by 24-25% (both on corporate and retail segment) vs the industry average growth by 20%. One of the assumptions of this aggressive growth is that debt capital markets will be closed or hard to access for Russian major corporates and they'll have to refinance the debt in the state banks as it was done in 4Q11.

We raise loan book growth forecast for FY11-12 due to strong performance in 11M11 and bank's management outlook

For our baseline scenario we increase our loan growth outlook in FY12 from 16% to 19%. We think that management's aggressive growth plans are too optimistic, taking into account: 1) expected Russian economy slowdown due to the deteriorating conditions in the global economy and therefore weaker demand on credit, 2) rising rates on corporate loans will also limit the demand on new loans, 3) the banks are likely to tighten the lending conditions due to the growing uncertainty in macro environment and borrowers financial position, 4) liquidity constraints, least painful for Sberbank, may limit the access to funding while the leverage of Sberbank (Loans/Deposits ratio) already exceeds 100%. The Minfin and Central Bank's funding is short-term and can hardly finance loan portfolio growth.

Sberbank management hopes to see some acceleration of the funding base growth as we expect the real interest rates on deposits to become positive in FY12. The bank plans to increase its market share in pension funds, payroll projects and mass affluent/affluent segments. Besides, bank CFO Mr Karamzin says that the leverage is in the comfortable zone and there's a reserve for loans growth provided by the change in the asset mix (as the share of loans increases at the expense of decrease in the share of securities portfolio).

3. Net interest margin

We leave our NIM FY11 outlook at 6.5% after strong 3Q figures (6.9%). Increased interest rates on retail deposits since November are unlikely to have an impact on NIM in 4Q, yet the bank's management acknowledges

Net interest margin (NIM) in 3Q peaked due to the lag effect from lowering cost of funding and increasing the share of high-yielding assets. In 4Q and 2012 we expect it to weaken due to rising cost of deposits and the pressure of low lending rates for large corporations

that the NIM may marginally decrease due to large refinancing of Russian blue chips dollar-denominated debt. Besides this segment, net interest spread increased in 4Q as the bank raised interest rates on corporate debt (except the largest corporate borrowers) by 100-150 b.p.

In 2012 the management expects NIM flat close to average FY11 level. We think it's possible although we see some risk of pressure on NIM in 1H12 as the deposits will be reprised by higher interest rates and this effect won't be fully compensated by the increase in the rates of corporate loans. In our model we expect NIM in 2012 around 6,4% and in 2013-14 – in the range 6,3-6,4%.

4. Cost of risk

The bank's management expects in the baseline scenario NPL share in corporate loan portfolio to diminish by approx. 0,9 p.p. due to aggressive loan book growth and partially – to the assets quality enhancement. In this scenario management estimates CoR close to 11FY level (about zero).

In the stress scenario (like 2008-09 for global economy) management hopes to see much softer influence of the external shocks to Russian economy. And in this case "the conservative" official estimate of CoR is "no more than 1%" – we remind that in 09FY it was about 7%.

We consider the management outlook on CoR as too optimistic, as some metals&mining companies (Rusal, Mechel) are already feeling the worsening global demand and market price conditions and are either negotiating with creditors on changing debt covenants or are at risk of their exceeding. We think that situation in global economy will continue to worsen at least in 1Q12 what may negatively affect the financial position and creditworthiness of some Russian corporate borrowers and make banks create provisions more conservatively. In the short term the influence of global economy problems on Russian economy seems to be moderate, but even in the baseline scenario we expect Sberbank CoR to reach 1-1,2% , which is yet lower than on average for Russian banking sector (1,5%).

We expect in our baseline scenario CoR in FY12 about 1,2%, which corresponds to Sberbank management stress scenario estimates

In the case the global economy conditions continue to deteriorate, putting pressure on China's economy and demand for wider range of commodities, including oil&gas (average oil price \$80-90 /barr), we expect CoR to return to 2% (FY10 – 2,6%). And it's not yet the worst stress scenario, comparable to 2008/09 turmoil.

In 2013-14 we imply conservative CoR assumptions – 1,5-1,3% as the global economy fragility is expected to continue for several years and is likely to affect Russian economy within a time lag as it happened during the Asian crisis (1997) and the last global crisis, which started for the foreign economies in 2007 but reached Russia only in the end of 2008. Even without the new serious shocks, the economy conditions are expected to be rather tight, so the borrowers' financial position is likely to remain under pressure.

We cut our operating costs forecast in FY12 from 16% to 13%

5. Operating costs

Management plans to restrict operation expenses seriously due to the cut of headcount (on average 5% on annual basis, which will be partially compensated by opening positions in new business lines) as well as to more efficient operation technologies. The bank's CFO A. Karamzin said that the operating costs growth will diminish from around 30% in 2011 to "low teens" in 2012.

We cut our costs outlook for FY12 from 16% to 13%, we expect low two-digit growth in the following 2 years.

6. Net income

So, Sberbank net income forecast for 2011 is raised by 8% (to 312 bln Rub), for 2012 - by 5% (to 272 bln Rub), for 2013 - by 4% (to 305 bln Rub). Only in 2014 we expect the net income to exceed the estimated 11FY record. The management's forecast is much more optimistic – they expect in the FY12 in the baseline scenario net income more than in FY11 (300-310 bln Rub)

	Old forecast, bln Rub	New forecast, bln Rub	Chg, %
2011F	288	312	8%
2012F	259	272	5%
2013F	292	305	4%
2014F		373	

Valuation

We estimate the fair value of Sberbank's shares based on the modified Gordon model (target P/BV) ($P/BV = (ROE - g) / (r - g)$).

Taking into consideration slower long-term growth expectations for Russian economy unless the significant structural reforms shifts its framework from the current (raw material export, import oriented consumption, huge budget expenses) to more efficient, intensive and diversified, we reduce the terminal growth rate (g) estimate from 6% to 5%. We leave the other key model parameters - 20% terminal ROE rate, 14% discount rate.

	2007	2008	2009	2010	2011F	2012F	2013F	2014F
Shareholders' capital, \$mln	25,959	25,533	25 758	32,391	39,750	45,041	53,452	66,558
Net income, \$ mln	4,165	3,940	770	5,992	10,662	8,448	9,464	11,462
Cost of equity, %						14.0%	14.0%	14.0%

Then, applying the Gordon model we obtain a target P/BV for 2014 of 1.7. Taking the forecast BV-2014 of \$66,558 mln, we obtain Sberbank's fair value at the end of 2014 to be $P-2014 = \$110 930$ mn.

Terminal ROE rate	20%
Terminal growth rate	5,0%
Target P/BV-2014	1.7
Fair MCap (P-2014), \$ mln.	110,930
Discount rate	14,0%
Fair MCap at the end of 2011, \$mln	74,874

Ordinary shares, mln	21,587
Preferred shares, mln	1,0
Fair value of 1 ordinary share at the end of 2011, \$	3.31
Fair value of 1 ordinary share in 12M, \$	3.77

Fair value of 1 ordinary share in 12M, \$:	3.77
Market price of 1 ordinary share (27.12.2011 r.)	2.57
Upside, %	47%
Recommendation	«Buy»

So far, **we increase the target price for Sberbank ordinary shares from \$3.45 to \$3.77 and reiterate recommendation «Buy»**. We estimate preferred shares with a 25% target discount to ordinary shares, so **target price for 1 pref share is \$2.83, which implies 48% upside to the market price, recommendation «Buy»**

- Market ratios for Sberbank (P/E 12E 6.6, P/BV 12E 1.2) look attractive compared to global peers (average EM P/E 12E = 7.2, P/BV 12E = 1.0), even according to our conservative outlook. Market consensus for Sberbank is P/E12 5.9, P/BV12 1.2. Sberbank now is trading with a premium to other Russian banks, for which MCap fell below 1.0 BV – nevertheless we think the premium is justified by the large capital adequacy ratio, favorable terms of access to liquidity, the stable funding base and the cheapest in Russia cost of funding. The key risk is Russian macro conditions deterioration. Among the potential drivers we see the possible privatization of CBR stake after presidential elections in March 2012.

Projected financial position, mn Rub

Balance, mln Rub	2009	2010	2011F	2012F	2013F	2014F
Cash and equivalents	725,521	719,601	647,787	757,910	804,551	917,188
Mandatory reserves	40,572	50,32	99,659	151,582	174,319	299,318
Securities	1,064,135	1,823,648	1,554,688	1,515,821	1,743,194	1,681,512
Loans to other banks	10,219	13,035	29,898	34,980	26,818	30,573
Loans and advances to customers	4,864,031	5,489,387	7,304,536	8,789,994	10,080,544	11,794,236
Premises and equipment	249,881	283,756	313,927	338,145	362,048	366,875
Other assets	150,707	248,568	15,453	71,727	217,710	196,768
Total assets	7,105,066	8,628,527	9,965,949	11,660,160	13,409,184	15,286,470
Due to other banks	53,947	188,431	392,122	458,226	409,081	396,895
Retail deposits	3,787,312	4,834,459	5,462,939	6,337,009	7,414,300	8,748,874
Corporate customers funds	1,651,559	1,816,672	1,943,839	2,196,538	2,460,123	2,730,736
Debt securities in issue	124,599	119,426	287,556	315,667	374,017	449,814
Other borrowed funds	115,23	270,765	261,415	305,484	385,705	515,964
Subordinated loans	519,061	303,513	318,147	318,147	318,147	-
Other liabilities	74,439	108,094	47,814	251,732	326,668	387,550
Total liabilities	6,326,130	7,641,360	8,713,833	10,182,803	11,688,042	13,229,834
Total shareholders' equity	778,936	987,167	1,252,116	1,477,357	1,721,142	2,056,636

Projected income statement, mn Rub

	2008	2009	2010	2011F	2012F	2013F	2014F
Interest income	619,952	814,962	795,646	846,603	1,073,395	1,221,919	1,385,586
Interest expenses	-241,795	-312,245	-299,825	-276,399	-419,645	-468,513	-518,577
Net interest income	378,157	502,717	495,821	570,204	653,750	753,406	867,009
Provisions charges for loans impairment	-97,881	-388,932	-153,809	1,567	-105,961	-149,795	-158,045
Net interest income after provision charges	280,276	113,85	342,012	571,771	547,789	603,611	708,964
Net Fee&Commissions	86,194	101,089	123,574	142,486	165,283	193,381	228,190
Operating income	360,524	259,141	512,754	756,256	753,072	839,993	980,154
Operating expenses	-221,739	229,277	-282,619	-365,992	-413,571	-459,063	-514,151
Pre-tax profit	138,785	29,864	230,135	390,265	339,501	380,929	466,003
Income tax expense	-32,175	-5,468	-48,487	-78,053	-67,900	-76,186	-93,201
Net income	97,746	24,396	181,648	312,212	271,601	304,743	372,803

Projected financial ratios

	2007	2008	2009	2010	2011F	2012F	2013F	2014F
Asset yield	11.2%	12.0%	13.3%	10.9%	9.7%	10.4%	10.3%	10.2%
Cost of funding	-4.8%	-4.7%	-5.1%	-4.4%	-3.4%	-4.5%	-4.4%	-4.3%
Net interest spread	6.4%	7.3%	8.1%	6.6%	6.2%	5.9%	5.9%	5.9%
Net interest margin	6.6%	7.3	8.2%	6.8%	6.5%	6.4%	6.3%	6.4%
ROE	22.1%	15.3%	3.0%	20.6%	27.9%	19.9%	19.1%	19.1%
ROA	2.5%	1.8%	0.3%	2.3%	3.6%	2.5%	1.8%	2.5%
Cost/Income	55.4%	48.4%	35.4%	42.4%	48.5%	48.1%	46.4%	45.2%
P/E	13.3	14.1	72.0	9.3	5.2	6.6	5.9	4.8
P/BV	2.1	2.2	2.2	1.7	1.4	1.2	1.0	0.8

Sources: company data, Sovlink

Stock recommendations

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:	Target price at or below current price levels

SOVLINK LLC

Tel.: +7 495 967-1300

Fax: + 7 495 967-1311

Kremlin embankment 1. bld. 2.

Moscow. 119019. Russia

www.sovlink.ru

research@sovlink.ru

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