

# Vakifbank

**Neutral**

Current price: 4,40 TL  
12-mo T.Price: 4,80 TL

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## 3Q14 Earnings Comment

3Q14 Actual result vs. estimates				Share Price performance		Margins	
TLmn	Actual	Cnbc-e	Ak				
Net Int.In.	1,195	-	1,193	1M		4.0%	
NIM	3.5%	-	3.5%	3M		3.0%	
Net Inc.	348	354	350	YtD		2.0%	
Sh.Equity	13,682	-	13,688			1.0%	
						0.0%	

### Key notes: RoE remained weak albeit an increase in NIM

- ✓ Vakifbank posted a 3Q14 net profit of TL348mn (almost the same as in 2Q14) and in line with our net profit estimate of TL350mn and the market consensus estimate of TL354mn. Thus, the bank's cumulative net profit for 9M14 came in at TL1,070mn, down by 7.8% YoY, with an RoE of 10.9% vs. 12.8% in 9M13.
- ✓ The solid performance in net interest income (albeit with the seasonally negative anomaly from CPI linkers) and commission generation in 3Q14 was not sufficient to lead to QoQ EPS growth, because of sizeable sum of non-recurring provision releases in 2Q14. Meanwhile, the bank's general provision burden in 3Q14, albeit on accelerated loan growth, was also milder than that of its peers, largely because of TL70mn in pre-loaded general provisioning set aside for the regulatory adjustment in 2Q14.
- ✓ Based on our calculation, the 11% QoQ increase in net interest income to TL1,195mn was completely thanks to a sharp fall in TL deposit costs and 28bps QoQ surge in the NIM to 3.5%. As such, the lower inflation proxy in 3Q14 (relative to 2Q) shaved TL106mn off its return on CPI linkers on a QoQ basis.
- ✓ Net NPL inflows in 3Q14 jumped to TL334mn, largely because of a slowdown in the collection performance due to seasonal factors, taking the bank's NPL volume to TL3.9bn with an NPL ratio of 3.9% (down 10bps QoQ) by the end of 3Q14. Meanwhile, the volume of Group II loans, which comprised 4.3% of the gross loan book, remained unchanged at TL4.3bn.

### Comment & rating:

- ✓ Our view on Vakifbank after the 3Q14 results remains neutral. We like Vakifbank's cautious provisioning policy which kept its NPL coverage at 94% (among the highest in the sector) and prevented the Bank from achieving a better RoE (contrary to some banks, which were able to report better results with an easing in their NPL coverage ratios). However, Vakifbank's RoA, despite its solid collection performance, still remains low and depresses its RoE. Following the release of the 3Q14 results, we cut our 2014 earnings forecast by 1.5% to TL1,475mn while raising our 2015 forecast by 3% to TL1,650mn. Our 12 month target price stands at TL4.80, offering 9% upside. We maintain a 'Neutral' rating for Vakifbank.

Key P&L items, TLmn	3Q14	3Q13	YoY Ch.	2Q14	QoQ chg.	9M14	9M13	YoY Chg.
Net Interest Income	1,195	1,076	11.0%	1,068	11.8%	3,274	3,536	-7.4%
Net Income	348	256	35.6%	349	-0.4%	1,070	1,161	-7.8%
Loans	97,398	81,927	18.9%	91,541	6.4%	97,398	81,927	18.9%
Marketable Sec.	22,556	21,378	5.5%	22,029	2.4%	22,556	21,378	5.5%
Core Deposits	85,303	74,513	14.5%	79,758	7.0%	85,303	74,513	14.5%
Shr. Equity	13,682	12,218	12.0%	13,496	1.4%	13,682	12,218	12.0%
NIM	3.5%	3.7%	-19bps	3.2%	28bps	3.2%	4.3%	-106bps
Cost of Risk	166bps	180bps	-14bps	201bps	-36bps	166bps	221bps	-54bps
NPL ratio	3.9%	3.9%	-8bps	4.0%	-10bps	3.9%	3.9%	-8bps
CAR	13.9%	14.3%	-43bps	14.3%	-42bps	13.9%	14.3%	-43bps
RoE	10.2%	8.5%	174bps	10.6%	-39bps	10.9%	12.8%	-198bps

## Analysis

**\* A resilient NIM in 3Q14** – Despite a TL106mn erosion in the bank's return on CPI linkers, largely because of a decline of around 100bps in average TL deposit costs (in contrast with a milder easing in TL loan yields), Vakifbank was able to improve its NIM by 28bps QoQ. The management expects a stable core spread in 4Q14 with an increase of around TL60mn in income from CPI linkers. Therefore, an increase of up to 10bps QoQ in the NIM in 4Q14 appears likely.

**\* A positive but slightly lower contribution from FX & trading gains** – Since Vakifbank is one of the few banks which do not utilize short term currency swaps to provide TL funding, its FX & trading gains of TL33mn largely reflected gains on bond trading and other Treasury operations (rather than swap costs). However, the TL50mn decline in this figure on a QoQ basis relative to 2Q14, when the Bank had recorded more trading gains, translates into a weaker contribution to the bottom line in 3Q14.

**\* Pre-loaded provisioning kept general provisioning low in 3Q14** – Vakifbank had set aside TL107mn of general provisioning in 2Q14, incorporating a TL70mn pre-loaded burden for the regulatory increase of the general provisioning rate on general purpose consumer loans. Thanks to the up-front provisioning in the previous quarter, Vakifbank's total general provisioning in 3Q14, despite a speed-up in loan growth, contracted to TL86mn (in contrast with the tendency at many of its peers).

**\* A decline in the NPL ratio despite a slowdown in NPL collections** – Vakifbank recorded TL159mn of net NPL entries in 3Q14, exceeding the TL129mn in 2Q14. However, because of the faster loan growth, the bank's NPL ratio contracted by 10bps QoQ to 3.9% by the end of 3Q14. Vakifbank has maintained its conservative approach with a policy of no NPL write-offs and its NPL coverage further increased by 74bps QoQ to 93.9%. As a result, the bank recorded specific provisions of TL305mn in 3Q14, keeping its gross specific CoR at 129bps (vs. 154bps in 2Q14). However, thanks to the strong NPL collection performance, the bank's net specific CoR remained at 65bps (56bps in 9M14). The bank does not expect any major hike in its provisioning burden in 4Q14 and maintains its net specific CoR guidance at 60bps.

**\* Solid performance in fees and commissions** – Despite negative seasonality in contributions from account maintenance fees, total net fees and commissions were up 17.7% QoQ in 3Q14, reflecting Vakifbank's accelerated loan growth in the quarter. Nevertheless, the cumulative figure in 9M14 was down by 1.8%. The management expects little or no change for the year end.

**\* Operating costs better than initial guidance** – Despite an additional burden of around TL71mn resulting from cancellations and back payments of some fees and commissions to customers (due to court rulings), the increase in operating costs in the first nine months of 2014 remained at 15.9%. The bank stated that the increase in operating costs for the 2014 full year would be lower than its initial guidance of CPI + 500bps, largely thanks to improved efficiencies achieved through retirements and other programmes.

**\* Loan growth driven by TL retail loans** – Vakifbank registered 3.5% QoQ loan growth on the TL side, mainly driven by SME lending. This was accompanied by 6.7% QoQ growth in FX loans (in US\$ terms), largely thanks to a US\$500mn project finance loan extended to Turkey's national oil company (TPAO) for the joint financing of its purchase of a 10% stake in Sahdeniz gas reserves and the South Caucasus gas pipeline.

**\* Strong growth in TL core deposits** – As far as funding was concerned, Vakifbank was more aggressive in deposit collection than in previous quarters and registered a solid 7.0% QoQ core deposit growth, mainly driven by FX retail deposits. In addition, the Bank also continued to expand its borrowing through bonds issues via private placements.

**\* Solvency ratios below the sector average** – As a result of the strong loan growth, Vakifbank suffered a 42bps QoQ erosion in its CAR to 13.9% by the end of 3Q14. Meanwhile, its Tier-1 ratio also contracted by 44bps QoQ to 11.1% by the end of 3Q14. Thus, both of its CAR and Tier-1 ratios are less than the depository banks' average respective ratios of 15.3% and 12.9%. Nevertheless, largely thanks to Vakifbank's selective use its capital, both of its solvency ratios at the end of 3Q14 were better than their levels at the end of 2013.

Income Statement (TL mn)	2Q14	3Q14	9M13	9M14	2013	2014F	2015F	2016F
<b>Interest Income</b>	<b>2,850</b>	<b>2,784</b>	<b>6,624</b>	<b>8,295</b>	<b>9,079</b>	<b>11,266</b>	<b>12,858</b>	<b>14,505</b>
- on TL loans	2,038	2,063	4,915	6,001	6,645	8,128	9,338	10,515
- on FX loans	247	293	671	796	919	1,121	1,482	1,861
- on TL securities	517	374	848	1,339	1,256	1,776	1,794	1,801
- other	48	53	189	159	258	241	244	328
<b>Interest Expenses</b>	<b>1,781</b>	<b>1,589</b>	<b>3,087</b>	<b>5,021</b>	<b>4,431</b>	<b>6,716</b>	<b>7,344</b>	<b>8,251</b>
- on TL deposits	1,168	1,057	2,115	3,308	3,041	4,433	4,912	5,256
- on FX deposits	117	101	279	341	393	457	573	767
- on borrowings & bonds	137	158	262	432	391	598	725	921
- other	359	272	431	940	606	1,227	1,135	1,307
<b>Net Interest Income</b>	<b>1,068</b>	<b>1,195</b>	<b>3,536</b>	<b>3,274</b>	<b>4,648</b>	<b>4,550</b>	<b>5,514</b>	<b>6,255</b>
FX & Trading Gains/Losses	80	33	206	186	232	216	100	80
Specific Loan Provisioning	349	306	986	926	1,260	1,278	1,464	1,606
Gen. Loan Provisioning	107	86	245	215	234	283	300	366
<b>Adj. Net Int. Income</b>	<b>693</b>	<b>836</b>	<b>2,512</b>	<b>2,319</b>	<b>3,385</b>	<b>3,204</b>	<b>3,850</b>	<b>4,363</b>
Fees & Commissions (net)	171	202	528	518	687	720	776	881
<b>Ordinary Income</b>	<b>864</b>	<b>1,038</b>	<b>3,040</b>	<b>2,837</b>	<b>4,071</b>	<b>3,924</b>	<b>4,627</b>	<b>5,244</b>
Other Income	387	200	524	811	708	1,047	889	935
Other Provisions	-3	19	130	51	164	71	75	80
Operating Expenses (-)	792	763	1,976	2,289	2,687	3,073	3,424	3,753
<b>EBT</b>	<b>461</b>	<b>456</b>	<b>1,458</b>	<b>1,308</b>	<b>1,929</b>	<b>1,827</b>	<b>2,016</b>	<b>2,346</b>
Dividends	1	0	54	66	54	66	70	75
Other Ext. Income/Loss	0	0	0	0	0	0	0	0
Tax (-)	113	108	350	303	397	418	436	545
<b>Net Profit</b>	<b>349</b>	<b>348</b>	<b>1,161</b>	<b>1,070</b>	<b>1,586</b>	<b>1,475</b>	<b>1,650</b>	<b>1,875</b>
<b>Balance Sheet (TL mn)</b>								
Cash & Equivalents	2,458	3,660	4,992	3,660	3,814	3,693	4,083	4,494
Reserve Deposits	17,466	18,125	13,693	18,125	17,793	18,570	19,858	21,270
Marketable Securities	22,029	22,556	21,378	22,556	21,692	22,498	23,560	25,032
TL	18,511	18,895	17,696	18,895	17,911	18,835	19,371	20,093
FX	3,518	3,661	3,682	3,661	3,781	3,663	4,189	4,939
Loans	91,541	97,398	81,927	97,398	86,496	100,938	117,169	136,495
TL	69,492	72,108	61,213	72,108	64,827	75,417	86,057	97,855
FX	22,049	25,290	20,714	25,290	21,670	25,521	31,111	38,640
Non-performing Loans	3,774	3,911	3,357	3,911	3,531	4,129	4,828	5,738
NPL Provisions (-)	3,516	3,672	3,121	3,672	3,275	3,798	4,454	5,308
Participations	1,538	1,532	1,443	1,532	1,611	1,532	1,532	1,532
Fixed Assets	1,469	1,525	1,292	1,525	1,332	1,525	1,525	1,525
Other (incl. leases)	1,779	2,231	2,003	2,231	2,501	2,369	2,686	2,939
<b>Total Assets</b>	<b>138,539</b>	<b>147,266</b>	<b>126,964</b>	<b>147,266</b>	<b>135,496</b>	<b>151,455</b>	<b>170,786</b>	<b>193,716</b>
Core Deposits	79,758	85,303	74,513	85,303	77,370	89,206	102,232	118,274
TL	59,401	62,120	55,740	62,120	58,050	65,155	74,148	82,978
FX	20,357	23,183	18,773	23,183	19,320	24,051	28,084	35,296
Bonds Issued	8,206	9,840	5,755	9,840	6,885	9,727	13,082	17,343
TL	2,134	2,454	2,488	2,454	2,355	2,495	2,821	3,146
FX	6,072	7,385	3,267	7,385	4,530	7,232	10,262	14,197
Wholesale Funding	10,573	11,303	10,423	11,303	11,405	11,074	11,803	12,941
Subordinated Debt	1,950	2,123	1,891	2,123	1,974	2,079	2,383	2,695
Repo & Interbank	17,340	17,747	15,408	17,747	18,639	18,191	18,579	18,041
Other	7,216	7,269	6,756	7,269	6,606	7,269	7,269	7,269
<b>Sh. Equity</b>	<b>13,496</b>	<b>13,682</b>	<b>12,218</b>	<b>13,682</b>	<b>12,616</b>	<b>13,908</b>	<b>15,438</b>	<b>17,154</b>
<b>Total Liabilities</b>	<b>138,539</b>	<b>147,266</b>	<b>126,964</b>	<b>147,266</b>	<b>135,496</b>	<b>151,455</b>	<b>170,786</b>	<b>193,716</b>

Composition of Assets & Liabilities	2Q14	3Q14	9M13	9M14	2013	2014F	2015F	2016F
Liquidity/Assets	2%	2%	4%	2%	3%	2%	2%	2%
Loans/Assets	66%	66%	65%	66%	64%	67%	69%	70%
Securities/Assets	16%	15%	17%	15%	16%	15%	14%	13%
Core Deposits/Assets	58%	58%	59%	58%	57%	59%	60%	61%
Repo & Interbank/Assets	13%	12%	12%	12%	14%	12%	11%	9%
Wholesale Funding/Assets	8%	8%	8%	8%	8%	7%	7%	7%
Leverage	10%	9%	10%	9%	9%	9%	9%	9%
Growth rates								
Net Interest Income	5.7%	11.8%	31.7%	-7.4%	18.9%	-2.1%	21.2%	13.4%
Specific Loan Provisions (-)	28.8%	-12.5%	126.1%	-6.0%	71.4%	1.4%	14.6%	9.7%
Adj. Net Int. Income	-12.3%	20.7%	13.2%	-7.7%	5.0%	-5.3%	20.2%	13.3%
Fees & Commissions (net)	18.1%	17.7%	88.7%	-1.8%	53.3%	4.9%	7.9%	13.5%
Ordinary Income	-7.6%	20.1%	21.7%	-6.7%	10.9%	-3.6%	17.9%	13.3%
Other Income	72.6%	-48.2%	3.5%	54.9%	13.4%	47.7%	-15.0%	5.2%
Operating Expenses (-)	8.0%	-3.6%	21.2%	15.9%	18.8%	14.3%	11.4%	9.6%
EBT	18.0%	-1.2%	17.7%	-10.3%	5.5%	-5.3%	10.3%	16.3%
Tax (-)	36.9%	-4.0%	22.6%	-13.4%	-6.6%	5.2%	4.3%	24.9%
Net Profit	-6.5%	-0.4%	15.0%	-7.8%	8.6%	-7.0%	11.9%	13.6%
Loans	0.0%	0.0%	14.0%	20.0%	13.0%	0.0%	0.0%	0.0%
Marketable Securities	0.0%	0.0%	9.0%	7.0%	9.0%	0.0%	0.0%	0.0%
Total Assets	0.0%	0.0%	5.0%	4.0%	4.0%	0.0%	0.0%	0.0%
Core Deposits	0.0%	0.0%	13.0%	8.0%	18.0%	0.0%	0.0%	0.0%
Sh. Equity	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Major Indicators								
NIM	3.19%	3.47%	4.3%	3.2%	4.1%	3.3%	3.5%	3.5%
Adj. NIM	2.1%	2.4%	3.1%	2.3%	3.0%	2.3%	2.5%	2.5%
TL Loan Yield	11.9%	11.7%	11.8%	11.7%	11.5%	11.6%	11.6%	11.4%
FX Loan Yield	4.5%	4.9%	4.9%	4.7%	4.8%	4.8%	5.2%	5.3%
TL Securities Yield	10.6%	8.1%	8.1%	9.9%	8.6%	9.7%	9.6%	9.4%
FX Securities Yield	5.2%	5.7%	5.0%	5.6%	5.2%	5.9%	5.5%	5.4%
Cost of TL Deposits	8.0%	7.0%	5.6%	7.5%	5.9%	7.3%	7.0%	6.7%
Cost of FX Deposits	2.2%	1.9%	2.2%	2.1%	2.3%	2.1%	2.2%	2.4%
RoA (annualized)	1.0%	1.0%	1.4%	1.1%	1.4%	1.1%	1.1%	1.1%
RoE (annualized)	10.6%	10.2%	12.8%	10.9%	13.0%	11.1%	11.3%	11.5%
Core RoE (annualized)	12.0%	11.5%	13.7%	11.5%	14.2%	12.0%	12.1%	12.2%
Cost/Income	47.0%	46.7%	39.8%	46.9%	41.5%	46.3%	46.3%	45.4%
Specific Gross Cost of risk	154bps	129bps	177bps	135bps	164bps	137bps	134bps	126bps
Overall Gross Cost of risk*	201bps	166bps	221bps	166bps	194bps	167bps	161bps	155bps
NPL ratio	4.0%	3.9%	3.9%	3.9%	3.9%	3.9%	4.0%	4.0%
NPL coverage	93.1%	93.9%	93.0%	93.9%	92.8%	92.0%	92.3%	92.5%
CAR	14.3%	13.9%	14.3%	13.9%	13.7%	13.6%	13.4%	13.0%
Tier-1 ratio	11.6%	11.1%	11.0%	11.1%	10.6%	10.9%	10.6%	10.2%
Loan/deposits	114.8%	114.2%	109.9%	114.2%	111.8%	113.2%	114.6%	115.4%

Source: Ak Investment, the ISE

\* quarterly growth rates for quarter figures & annual growth rates for cumulative figures

\*\* (specific + general loan provisions)/avg. loans

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