

22 March 2011

# Portuguese Banks: to reach an 8% CT ratio by YE11

(Price Target and Recommendation maintained)

## 8% CT1 ratio for all...

According to the update of the Portuguese Growth and Stability Pact (GSP) presented yesterday, Portuguese banks must have an 8% CT1 ratio by YE11. According to the document, bank will have to present a until the end of May a reorganization plan. Such plan should define target and timeframe for the size and composition of the B/S, capital ratios and efficiency levels.

## Restore confidence in Portuguese banks seems to be the goal...

Earlier this month, in the Finance Ministry presentation of the revised GSP, it was mentioned that banks would have to prepare reorganization plans. The purpose of such plans is to reinforce Portuguese banks capital, considering the required deleverage of the financial system and the need to regain access to funding markets. Such plans will be evaluated by the BoS until the end of May.

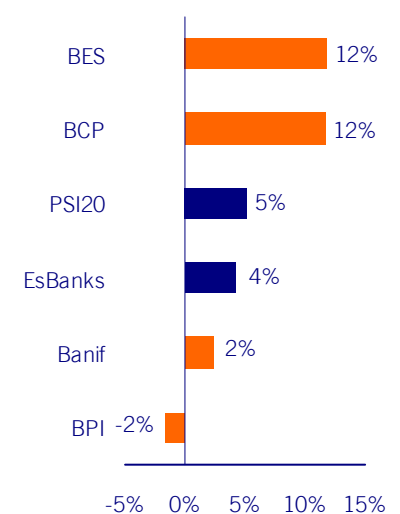
## Will these measures go through?

These capital requirements are part of the updated SGP. The leaders of the major opposition parties have stated that their parties will vote against the SGP in the Parliament in what may be the trigger for a political crisis and early elections in the country. That said the reason behind the opposition veto is not related with the higher capital ratios demanded to banks, but with the new austerity measures foreseen in the document, which makes us believe that these measures will be eventually imposed to banks.

## BCP and BNF as the most penalized

Looking at the listed Portuguese banks capital position as of Dec10, BCP and Banif should face the most challenging task to fit to the 8% CT1 threshold: (1) BCP posted a CT1 ratio of 6.7% at YE10, implying a gap of Eur 800mn (26% of current mkt cap); (2) Banif faces a gap of Eur 85mn (17% of mkt cap), from a CT1 of 7.3% at YE10; (3) BES is also slightly below the 8% threshold, but the 10bps gap (or Eur 100mn, 3% of mkt cap) should be manageable in the short-term thought retained earnings

Portuguese Banks - Market performance (YTD)



Source: Bloomberg

## Summary of Recommendations

Bank	Last price 21-Mar	Mkt Cap (Eur bn)	Price Target	Upside	Recom.	Adj. PE11F	Adj. PBV11F	DY11F
BES	3.22	3.8	3.15	-2%	Accu.	9.6	0.7	5.5%
BCP	0.65	3.1	0.60	-8%	Hold	14.8	1.1	0.0%
BNF	0.89	0.5	0.90	1%	Hold	12.9	0.6	2.6%
BPI	1.36	1.2	N.R.		N.R.	7.4	n.a.	n.a

Source: BPI Equity Research.

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**Portuguese Banks - Potential capital Needs**

Eur mn	BCP	BES	BPI	BNF
Core Capital	3 966	5 407	2 267	934
Tier 1	5 455	6 031	2 379	1 079
RWA	59 564	68 839	26 031	12 736
Core capital Ratio	6.7%	7.9%	8.7%	7.3%
Tier 1 ratio	9.2%	8.8%	9.1%	8.5%
<b>Capital required to reach a 8% CT1</b>	<b>799</b>	<b>100</b>	<b>0</b>	<b>85</b>
<b>% of mkt cap</b>	<b>26%</b>	<b>3%</b>	<b>0%</b>	<b>17%</b>
Pension fund Corridor	532	218	234	14
post tax	391	160	172	6
Other actuarial losses not recognised in capital	267	269	0	0
post tax	196	198	0	0
CT1 after deduction all PF losses	3 379	5 049	2 095	927
CT1 ratio	5.7%	7.3%	8.0%	7.3%
<b>Capital required to reach a 8% CT1</b>	<b>1 386</b>	<b>458</b>	<b>0</b>	<b>92</b>
<b>% of mkt cap</b>	<b>45%</b>	<b>12%</b>	<b>0%</b>	<b>18%</b>
<b>Per each 100bps k increase</b>				
<b>EPS dilution</b>				
	2011	-18%	-13%	-14%
	2012	-18%	-13%	-18%
	2013	-18%	-14%	-19%

Source: BPI Equity Research

**BCP: an equity-per-debt operation as a possibility**

BCP posted a CT1 ratio of 6.7% at YE10, implying a gap to the 8% CT1 threshold of Eur 800mn (26% of current mkt cap). In the earnings presentation, management mentioned an equity-per-debt operation as a possibility to enhance mentioned an equity-per-debt operation as a possibility to enhance capital ratios. We believe it would likely be the optimal solution both for the bank and the holders of the prefs. For the bank this would allow minimizing the EPS dilution and the discount at which the new shares are issued vs. a rights issue, given that this debt is trading significantly below its nominal value. For the holders of this debt issues, it could be the way of cutting losses.

For illustration purposes, **we estimate a 12% EPS dilution in a medium-term for a swap of Eur 750bn of prefs shares (25% of current # shares).**

To go through, such operation would have to be approved in BCP's GSM and the bank would then launch a tender offer over those securities.

**BCP: impact from the conversion of T1 perpetual debt into Equity**

Eur mn	2011	2012	2013
<b>Prior debt per Equity</b>			
# shares	4 695	4 695	4 695
NP estimate (as reported)	305	412	513
Cost o prefs	49	49	49
cost of T1 perpetual debt	50	50	63
<b>Adj. NP</b>	<b>206</b>	<b>313</b>	<b>401</b>
Adj. EPS	0.044	0.067	0.086
After debt swap			
# shares	5 848	5 848	5 848
NP estimate (as reported)	305	412	513
Cost o prefs	12	12	12
cost of T1 perpetual debt	50	50	63
<b>Adj. NP</b>	<b>242</b>	<b>350</b>	<b>438</b>
Adj. EPS	0.041	0.060	0.075
EPS accretion (/dilution)	-5%	-10%	-12%

Source: BPI Equity Research

**BCP: impact from the conversion of T1 perpetual debt into Equity**

Eur mn	Dec10
<b>Prior debt per Equity</b>	
CT1	3966
Tier 1	5455
RWA	59564
CT1	6.7%
Tier 1	9.2%
Debt converted	750
<b>Prior debt per Equity</b>	
CT1	4716
Tier 1	6205
CT1	7.9%
Tier 1	10.4%

Source: BPI Equity Research

**BCP: Relative valuation before and after the operation**

	2011F	2012F	2013F
<b>Prior to the operation</b>			
EPS	0.044	0.067	0.086
Adj. BV	2808	3047	3187
Adj. BVPS	0.60	0.65	0.68
Adj PBV	1.09	1.00	0.96
PE	14.83	9.73	7.60
<b>Adjusted for the K increase and MCB issue</b>			
EPS	0.041	0.060	0.075
Adj. BV	3558	3797	3937
Adj. BVPS	0.61	0.65	0.67
Adj PBV	1.07	1.00	0.97
PE	15.7	10.9	8.7

Source: BPI Equity Research

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	Low Risk	Medium Risk	High Risk	As of 28 <sup>th</sup> February BPI Equity Research investment ratings were as follows:
Buy	> 15%	>20%	>25%	Buy 36%
Accumulate	>10% and < 15%	>10% and < 20%	>15% and < 25%	Accumulate 24%
Hold	>0% and < 10%	>0% and < 10%	>0% and < 15%	Hold 22%
Reduce	>-15% and < 0%	>-20% and < 0%	>-25% and < 0%	Reduce 13%
Sell	< -15%	< -20%	< -25%	Sell/Accept Bid 4%
				Under Revision 1%
				Total 100%

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