8 December 2017

BANKING SECTOR REPORT – NOVEMBER 2017

EXECUTIVE SUMMARY

In November, US Banks increased by 3.1% MoM vs +2.8% MoM of S&P 500 Index after the flat performance (vs SPX index) in the previous month. Despite strong performance of banks in the last 3 month, SPX still continues to outperform financial sector YTD: +18.3% vs +13.9% of BKX index. Absolute November performance on MoM basis was just +0.35 StD from the mean monthly performance and this result is in the top 36% of absolute monthly performance of BKX Index. Relative November performance vs SPX index was +0.3% MoM in absolute terms, it is +0.05 StD from the mean, and this result is in the top 46% of relative performance of BKX index vs SPX.

Dynamics of the sector was driven by progress in the tax reform, Powell's testimony, deregulation optimism and expectations of December hike. The most impressive dynamics was demonstrated by SYF, RF, CFG and ZION. FRC, COF and BBT performed relatively weak during the last month.

Recently, the odds to complete tax reform in the near future have significantly increased due to approval of the bill in the House and successful talks in the Senate, so banks positively reacted to this news. The tax reform is surely a good driver of EPS growth, even despite the proposed lowering the statutory federal corporate tax from 35% to 20% is markedly below than the initial Trump's promise of lowering it to 15%. The Powell's testimony, where he said that the regulation was already tough enough and that banks weren't still too big to fail, was interpreted as the sign of the further deregulation. It was also positively impacted on banking quotes. The uncertainty around the final version of tax reform is still relatively high (even timing, at least timing of effective date of lowered tax rate) and we don't exclude temporary correction in US financial sector in case of some problems with the reform enactment and some changes compared to the House version of the bill. But we consider this scenario as a buy opportunity even despite rich valuations, because fundamentals of US banks still remain valid while tax reform and deregulation should be strong positive driver for operating results of US banks.

As was widely expected, the FOMC left the Fed funds rate unchanged at the November meeting, which was held on November 1. Overall, there were almost no changes in the statement. But taking into account recent macro data and the minutes from the November FOMC meeting, there is little doubt that FOMC will not hike rate at the December meeting (December 13). Currently, the market estimates the probability of the event at 98.3% vs around 20% as start of September. Despite the majority of the FOMC members consider current low inflation as temporary event, the minutes contained quite a long discussion about low inflation. In turn, inflation estimates were slightly revised down and it was noted that core inflation remained soft. Also, the wording about growth of the economy was changed to "solid" from "moderate". Overall, the FOMC meeting announcements are quite positive for operating results of US banks as rates will probably continue to rise but it seems that it has already been largely priced in. Moreover, deposit beta has begun to grow fast enough recently. Currently, it is around 40% at some banks. Of course, average beta is still significantly below levels of the previous cycles, but it has already started negatively impact on NIM growth. The other problem is flattening yield curve that fully complies with the previous Fed tightening cycles when the yield curve flattened during the rate hike cycle. 10yr-2yr spread continues to go down and currently it is near the lowest level since 2007.

Macro data was strong in November. Citi economic surprise index continued to go up. It increased by 19.2 pts MoM to +59.4 pts in November, the highest level in more than 3 years. The index returned on the positive territory in the early October and it continued to grow in early December. But banks go on to tighten credit standards in many segments. The October 2017 Senior Loan Officer Opinion Survey indicated that C&I lending standards were modestly eased to both small firms, large and middle-market firms over the past three months. Technically, banks slightly eased standards in C&I for the third consecutive quarter after tightening standards 6 quarters in a row. More aggressive competition from other banks was by far the most emphasized reason for easing. Notwithstanding, banks continue reporting weaker demand. CRE lending standards were tightened for the ninth consecutive quarter. Banks also reported that demand for CRE loans was weaker during the last quarter. All surveyed categories of mortgage lending either eased or remained basically unchanged over the past three months. Lending standards for consumer loans were tightened in the last three months. Specifically, standards were tightened in Credit Cards and Auto loans while standards for other consumer loans were basically unchanged. “Major shares of banks reported that a less favorable or more uncertain economic outlook, a deterioration or expected deterioration in the quality of their existing loan portfolio, and a reduced tolerance for risk were important reasons for tightening their standards or terms on credit card and auto loans to prime and subprime borrowers”.

In November EU Banks decreased by 2.1% MoM vs -2.2% MoM of STOXX 600 Index. It is the third month in the last four ones of the negative dynamics for European banks. However, banks were flat YTD vs broad based market index to the current time. EU banks continue trading in the narrow sideway channel for more than 7 months (175-191 pts on the SX7P index). Absolute November performance of SX7P was -0.39 std from the mean and this result is in the bottom 29% of absolute monthly performance of SX7P since the index inception. Relative performance of SX7P in November was around 0%.

Dynamics of European banks wasn’t uniform in November. The key underperformers were French banks because of relatively weak 3Q17 earnings in the early November. BPE added around 10% in November after the weak performance in October. Among banks with the best performance are also DBK and CS, which are the biggest European beneficiaries of possible deregulation and the tax reform in US.

Steady economic expansion in the euro area continues with GDP YoY growth higher than 2% and recent macro data indicates that it will remain solid in 2H2017. The second estimate of 3Q17 EU aggregate GDP growth was +0.6% QoQ and +2.5% YoY. We don’t exclude some deceleration of growth of EU economy because of euro strengthening, but it should still remain supportive for quotes of European banks in near years given the broad-based and self-sustained character of the current stage of recovery of the European economy. Eurozone GDP growth consensus was revised up by 10 bps for 2017 (to 2.2% yoy from 2.1% yoy 1 month ago), estimates of GDP 2018 was also revised up by 10 bps to 1.9% in the Bloomberg’s November survey while consensus estimate of 2019 GDP growth was unchanged at 1.6%.

EU rates were relatively flat in November because of dovish results of the October ECB meeting. The yield curve continues to become steeper, but given the market expectations, the first rate hike will not happen earlier than in 1H2019, from our point of view, and negative deposit facility rate environment will persist at least until the middle of 2020. Growth of the long yield hasn’t transformed into growth of back book yields yet. So, we still think that it is too early to buy EU banks because of possible rising rates in future given very strong outperformance of European banks in the last year. Of course, fundamentals will continue gradually improve but the short end of the curve will not change significantly until the key policy rates will eventually start to grow; low rate environment will persist for several more years; growth of long end is largely already priced in, from our point of view; valuations don’t look as reasonable as before; loan growth is still sluggish, especially in corporate segment while credit quality issues remain.

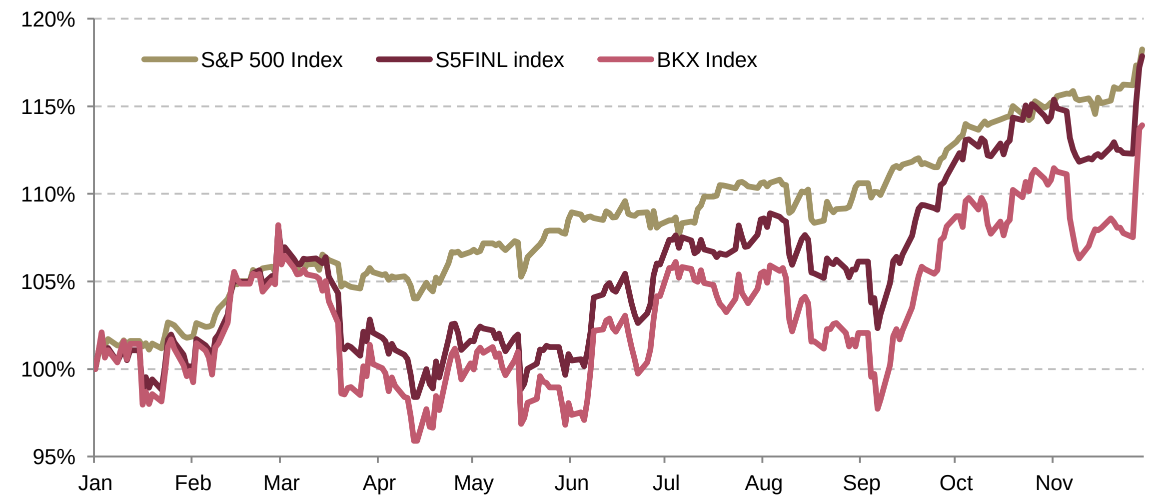
1. MARKET PERFORMANCE

US

In November, US Banks increased by 3.1% MoM vs +2.8% MoM of S&P 500 Index after the flat performance (vs SPX index) in the previous month. Despite strong performance of banks in the last 3 month, SPX still continues to outperform financial sector YTD: +18.3% vs +13.9% of BKX index. Absolute November performance on MoM basis was just +0.35 StD from the mean monthly performance and this result is in the top 36% of absolute monthly performance of BKX Index. Relative November performance vs SPX index was +0.3% MoM in absolute terms, it is +0.05 StD from the mean, and this result is in the top 46% of relative performance of BKX index vs SPX.

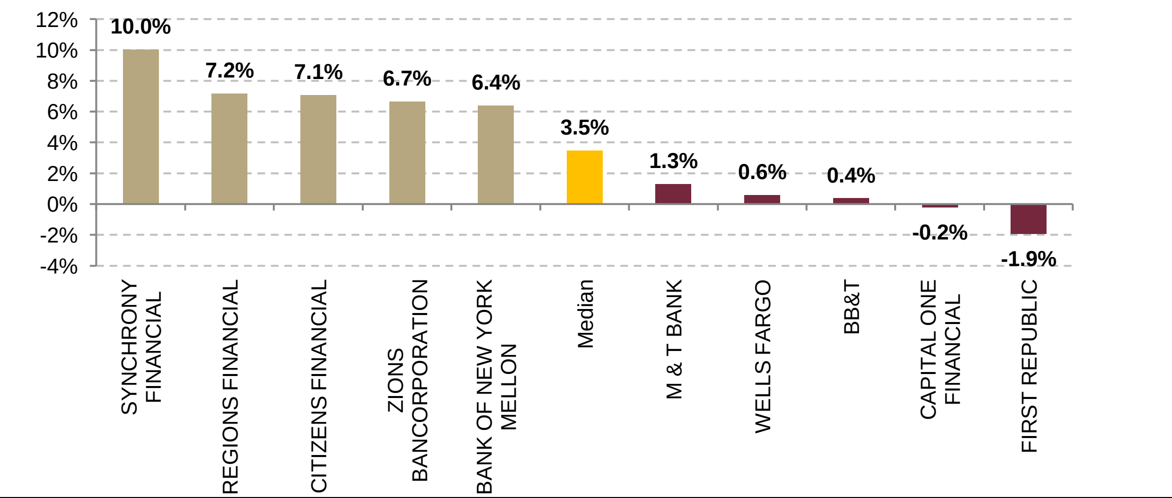
Dynamics of the sector was driven by progress in the tax reform, Powell's testimony, deregulation optimism and expectations of December hike. The most impressive dynamics was demonstrated by SYF, RF, CFG and ZION. FRC, COF and BBT performed relatively weak during the last month.

Chart 1. US Banks Performance. BKX Index vs S&P500 & S5FINL Indexes



Source: Bloomberg

Chart 2. November US Banks Performance. Leaders and Laggards, 1Month Performance,%



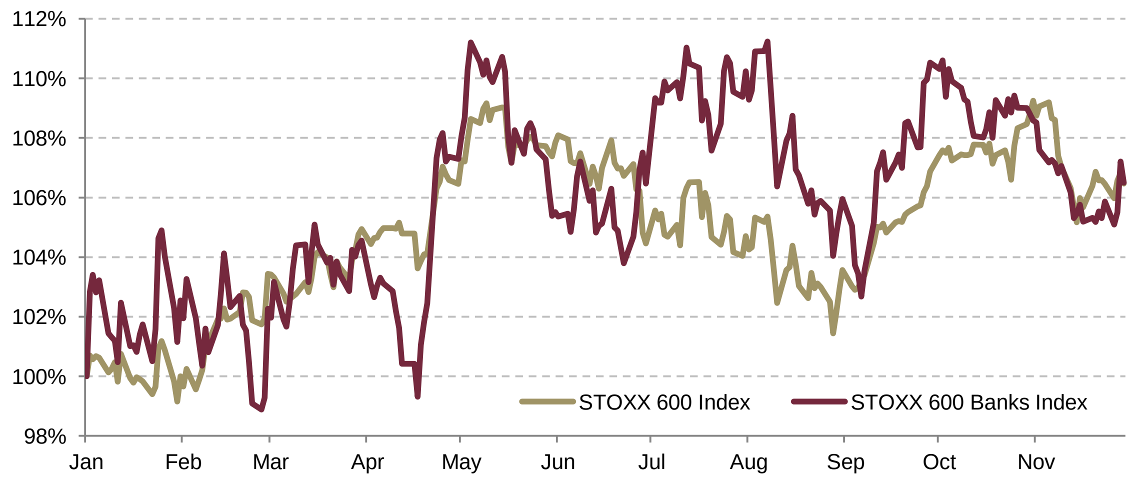
Source: Bloomberg

Europe

In November EU Banks decreased by 2.1% MoM vs -2.2% MoM of STOXX 600 Index. It is the third month in the last four ones of the negative dynamics for European banks. However, banks were flat YTD vs broad based market index to the current time. EU banks continue trading in the narrow sideway channel for more than 7 months (175-191 pts on the SX7P index). Absolute November performance of SX7P was -0.39 std from the mean and this result is in the bottom 29% of absolute monthly performance of SX7P since the index inception. Relative performance of SX7P vs STOXX 600 index in November was around 0%.

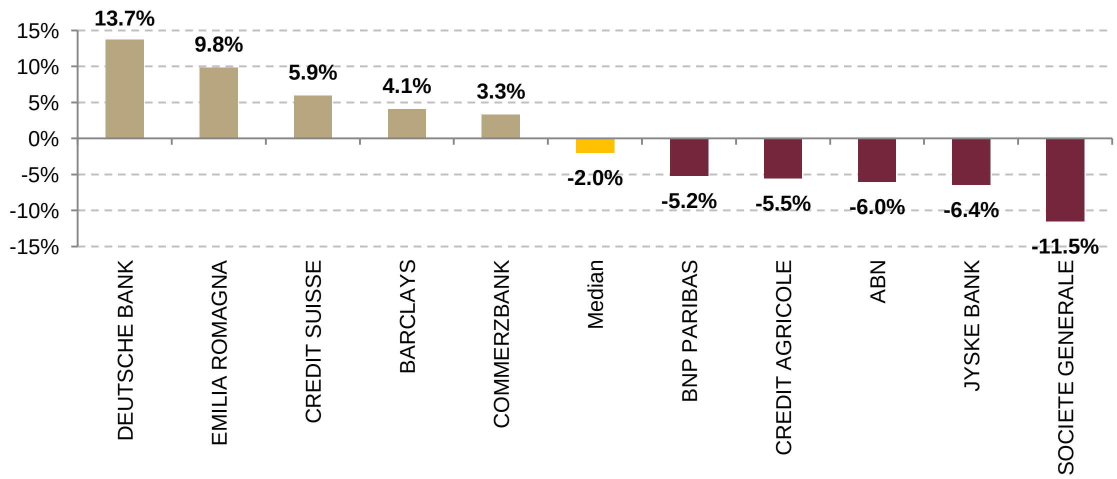
Dynamics of European banks wasn't uniform in November. The key underperformers were French banks because of relatively weak 3Q17 earnings in the early November. BPE added around 10% in November after the weak performance in October. Among banks with the best performance are also DBK and CS, which are the biggest European beneficiaries of possible deregulation and the tax reform in US.

Chart 3. EU Banks Performance. SX7P Index vs STOXX 600 Index



Source: Bloomberg

Chart 4. November EU banks performance. Leaders and Laggards, 1Month Performance,%



Source: Bloomberg

2. COMPANY NEWS

Societe Generale Investor Day

Societe Generale (GLE FP) released its business plan to 2020 on November 27. On November 28, it also held the Investor Day, presenting its new targets. 2020 Group financial targets are following: more than +3% revenue CAGR; 2020 costs not higher than €17.8 bn; ROTE around 11.5%; fully-loaded CET1 ratio not lower than 12%; around 3% RWA CAGR; cost income ratio less than 63%; EPS around €6.5; leverage ratio between 4% and 4.5%; progressive growth of the dividend, with a 50% payout ratio and a floor at EUR 2.20 per share, which will apply from 2017. Overall, the figures are ambitious and the key risk is execution. Currently, Bloomberg 2020 EPS consensus estimate is 10% below than the mgmt target. Moreover, it decreased by 2% after the presenting of new business plan. The market perception of the event was clearly negative as GLE decreased by 2.8% during the last four trading days of November vs +0.6% of SX7P index. GLE was the worst performer among European banks in November, -11.5% MoM vs -2.1% MoM of SX7P.

GLE's figures look ambitious, especially in terms of revenues given weak track record and cost targets. From our point of view, current revenue targets look unattainable without marked acceleration of NII growth which highly depends on growth of the key ECB rate. We don't expect that the ECB will hike rate earlier than 1H2019. In any case, the market prefers to see execution firstly to improve its EPS forecasts. Cost targets look more reasonable (including further both branch and headcount reduction), but final C/I figure, which should decrease from 68% in 2016 to 63% in 2020, also depends on revenue growth. Moreover, cost savings imply cumulative investments of €1.5 bn in 17-20 yrs and it will translate into €0.4 bn of one-off charge, which will be booked in 4Q2017.

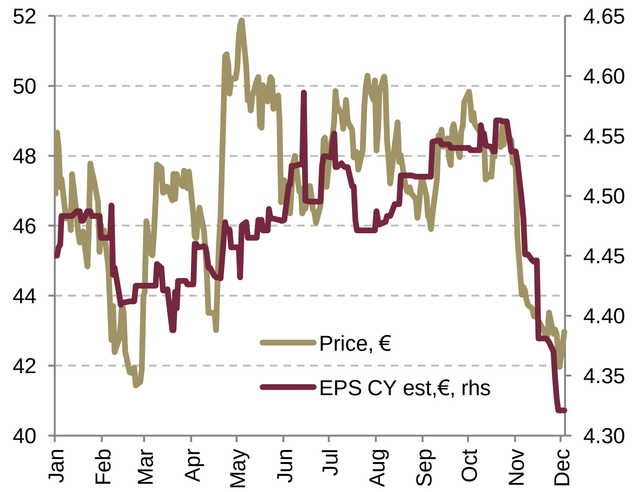
We see upside potential in GLE, but momentum is negative for the stock at the current time. We think that there is a risk of further decreasing of quotes (to €37.5), so it is not the best moment to buy the stock. Current GLE's P/B is 0.6x with consensus 2019E ROE of 7.5% vs 1.0x of EU banks and 9.0% ROE estimates. P/E 17E & 18E are 10.0x and 9.3x respectively vs 11.8x & 10.5x for EU banks. We are Neutral on GLE and we prefer BNP in France due to its better diversification and higher upside. Our price target for GLE is €52.5.

Table 1. GLE's 2020 targets

	2020 targets
Revenue growth, CAGR	> +3%
Costs, € bn	< 17.8
ROTE	~11.5%
CET1 ratio, fully-loaded	≥ 12%
RWA growth, CAGR	~3%
Cost/Income ratio	< 63%
EPS, €	~€6.5
Leverage ratio	4.0%-4.5%
Dividend floor, €	2.2

Source: Bloomberg

Chart 5. GLE. Price vs EPS estimates



Source: Bloomberg

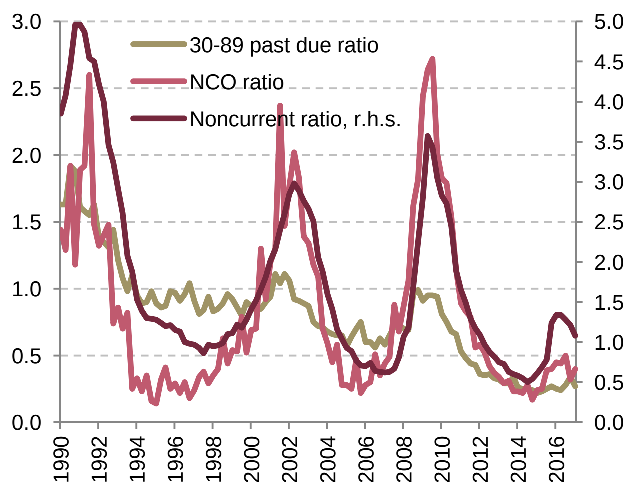
3. MACROECONOMIC NEWS

US

C&I loans

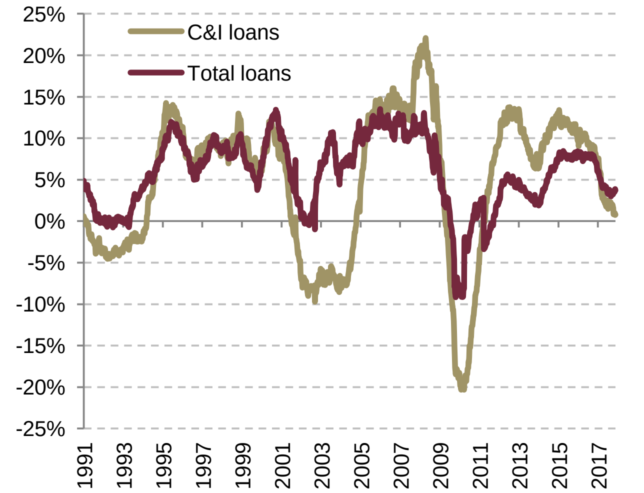
C&I loan growth continues to weaken despite some progress regarding tax reform, easing lending standards for the third consecutive quarter and still solid macro figures. During the last earnings season, banks named the same reasons of the slowdown as before – 'wait and see' approach of borrowers because of lack progress in reforms and switching of the large borrowers to capital markets. The new one was temporary run-off of the loan portfolio. Notwithstanding, mgmt of banks still remains optimistic regarding further C&I growth after successful implementation of the promised reforms. However, the same optimism had been demonstrated in the beginning of the year, but the loan growth rate continued to go down then. According to the last Fed H8 weekly report, C&I loan growth slowed down to just +0.8% yoy (for the week ending November 22) vs +2.1% yoy (as the end of 3Q17) and +7.9% yoy as of 23 November 2016.

Chart 6. C&I. Delinquencies vs NCOs, %



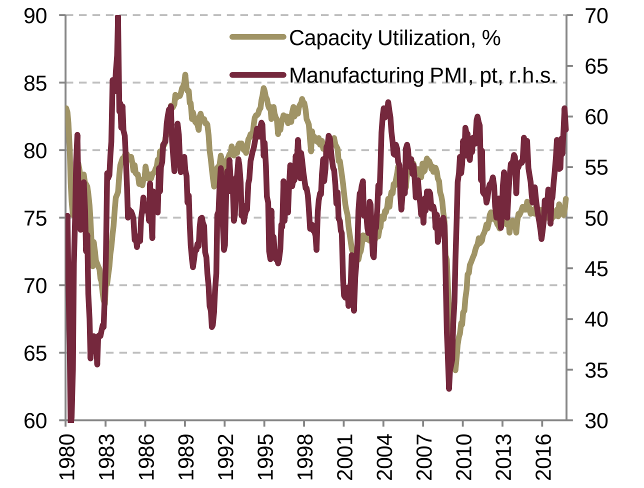
Source: Bloomberg

Chart 7. Loan Growth. C&I vs Total loans, YoY%



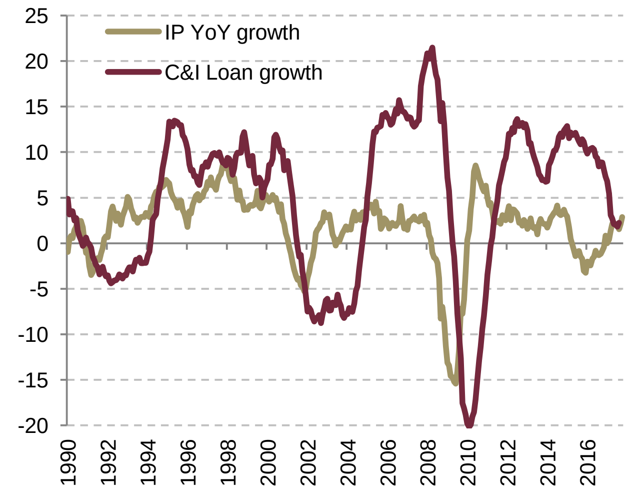
Source: Bloomberg

Chart 8. C&I. Manuf. PMI vs Capacity Utilization, %



Source: Bloomberg

Chart 9. C&I. Ind. Production vs Loan Growth YoY%



Source: Bloomberg

We make no question of the acceleration of growth of the loan portfolio from current levels, however, we do not expect that it will be significantly higher than the growth rate of nominal GDP. The October 2017 Senior Loan Officer Opinion Survey indicated that C&I lending standards were modestly eased to both small firms, large and middle-market ones over the past three months. Technically, banks slightly eased standards for the third consecutive quarter after tightening standards 6 quarters in a row. More aggressive competition from other banks was by far the most emphasized reason for easing. Notwithstanding, banks continue reporting weakening demand. “Demand from large and middle-market firms weakened, while demand for such loans from small firms was reportedly unchanged on net”. “Meanwhile, inquiries from potential business borrowers regarding the availability and terms of new credit lines or increases in existing lines reportedly remained basically unchanged over the past three months on net”.

Macro was strong so far in November due to recovering of some data after negative readings in the previous months because of adverse impact of the hurricanes Irma and Harvey. Better than estimates figures were demonstrated by construction spending, manufacturing payrolls, factory orders, industrial production and leading economic index. In turn, ISM manufacturing, Empire manufacturing and NFIB small business optimism indexes were worse than expectations. However, Citi economic surprise index added +18.3 pts since the end of October (as of November 21), the highest level in more than 3 years.

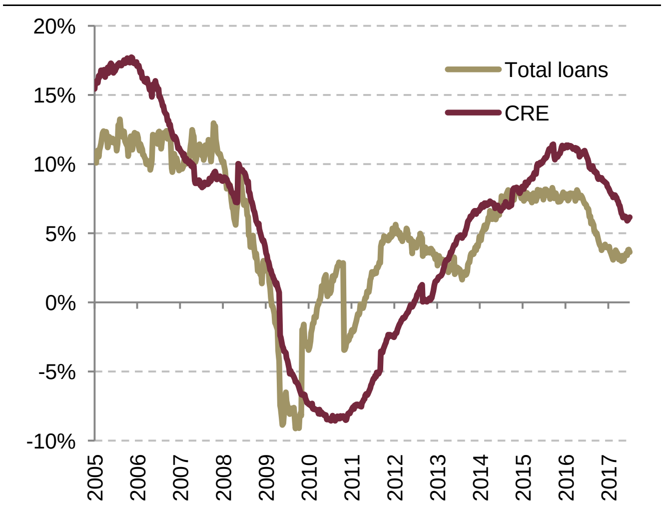
ISM manufacturing index decreased by 2.1 pts MoM to 58.7 pts in October vs expectations of 59.5 pts. But it remains near the highest level in more than 13 years. Manufacturing payrolls increased by 24k in October vs expectations of growth of +15k. Moreover, September’s figure was revised up from -1K to +6K. Construction spending increased by 0.3% MoM in September vs expectations of -0.2% MoM. However, August figure was revised down from +0.5% to +0.1% MoM growth. Factory orders increased by 1.4% MoM in September vs expectations of +1.2% MoM after solid growth of +1.2% in August. Industrial production spiked by +0.9% MoM in October, significantly beating expectations of +0.5% after relatively weak growth in the previous months (in the first place in August) because of the negative hurricanes impact. In turn, Empire manufacturing index was weak in October, decreasing by 10.8 pts to 19.4 pts, being significantly lower than estimates of 25.1 pts. But overall, macro data continues to indicate healthy growth of manufacturing but this growth couldn’t transform into strong rate of increase of C&I loans yet due to the policy uncertainty.

CRE

Commercial real estate still remains one of the fastest growing segment in US (+6.2% yoy through November 22th vs 3.7% yoy growth for total loans), but growth rate continues to decelerate (+11.1% yoy as the beginning of November 2016). CRE added 5.7% YTD vs +9.3% for the same period of 2016. Sector fundamentals remain relatively strong, but we continue to see more and more signs of imbalance. Price growth accelerated in the last months to 7.5% yoy as end of September 2017 while transaction volumes were weak in 2017 (-7.3% yoy as the end of September), operating fundamentals are starting to lag behind prices and banks continue to tighten lending standards (for the ninth quarters in a row). From our point of view, it suggests that we are at a late stage of the cycle, although quality indicators still continue to improve.

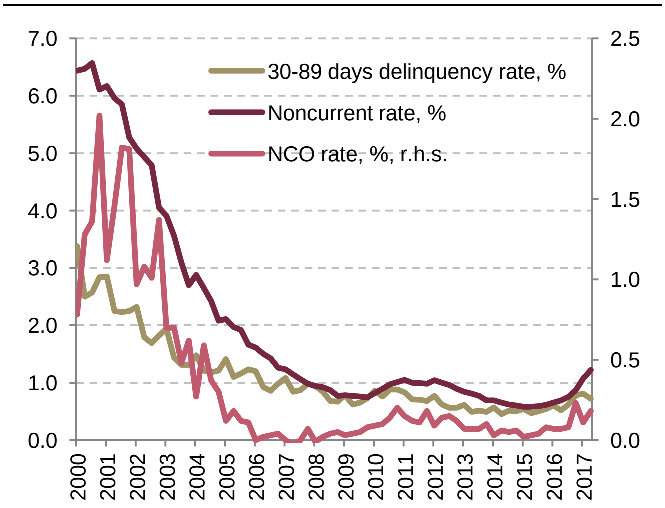
The October Senior Loan Officer Survey indicated that CRE lending standards were tightened for the ninth consecutive quarter. “A significant net fraction of banks reported tightening their standards for loans secured by multifamily residential properties, while banks reportedly left standards for loans secured by nonfarm nonresidential properties and those for construction and land development purposes basically unchanged on net". Banks also reported that demand for CRE loans was weaker during the last quarter. Weaker demand was demonstrated by all major CRE segments (moderate for multifamily and modest for construction and for nonfarm nonresidential properties). "In contrast to domestic respondents, a moderate net share of foreign banks indicated that demand for CRE loans strengthened in the third quarter". Given a relatively strong correlation of tightening standards and deterioration of asset quality, ongoing growth of rates in the economy and the record level of prices, CRE could potentially have a negative impact on quality of the overall loan portfolio of US banks. But we expect that the impact will be limited because of low LTV ratios and relatively strict lending standards during the last credit cycle.

Chart 10. Loan Growth. CRE vs Total Loans, YoY, %



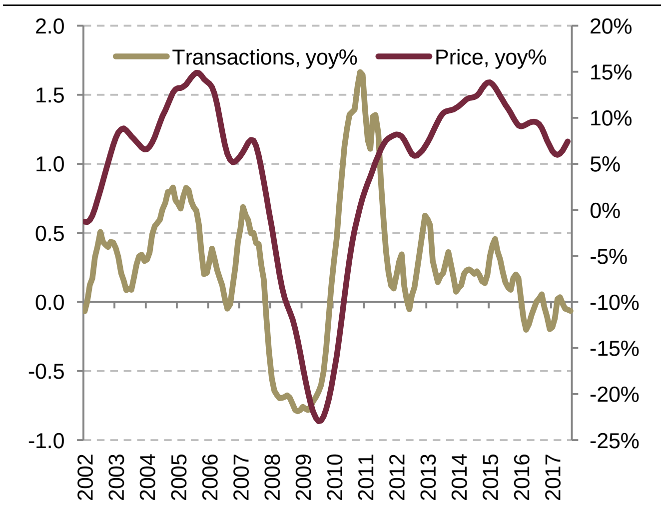
Source: Bloomberg

Chart 11. CRE. Delinquencies vs NCOs, %



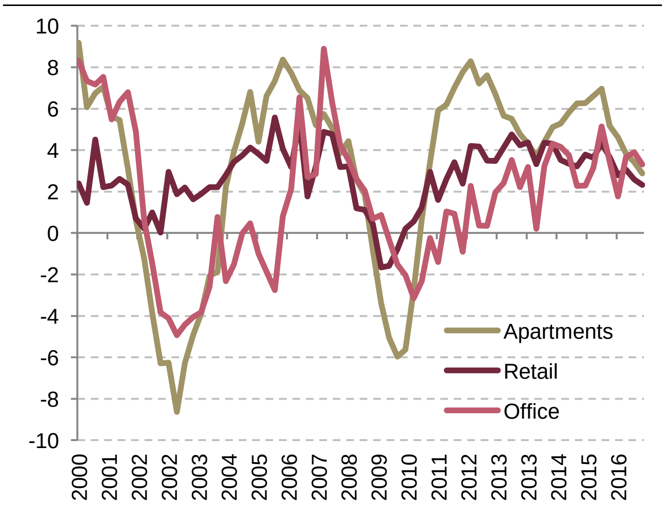
Source: Bloomberg

Chart 12. CRE. Price Growth vs Transactions Volumes



Source: Bloomberg

Chart 13. CRE. Same-Store NOI Growth, %



Source: Bloomberg

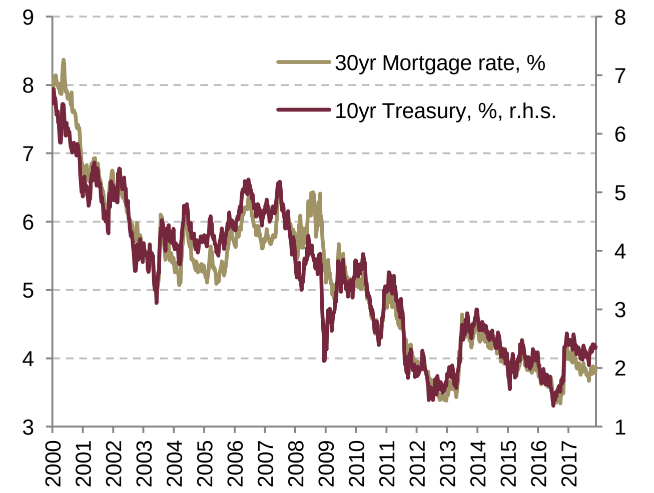
Overall, business cycle remains supportive for commercial real estate segment even taking into account significant growth yields from the lows of 2016. The Moody's Commercial Property Price Index (CPPI) markedly accelerated in the last months adding more than 5% since the end of March 2017, due to acceleration of prices growth in apartments and office segments. In turn, retail segment remains weak showing just +0.8% yoy growth of prices as the end of September 2017. It seems that recent concerns about e-commerce competition weren't unfounded. Current growth of CRE prices is markedly lower than it was few years ago, but it is still significantly higher than growth of housing prices. It seems that the lack of the growth of rates in the beginning of the year and seasonality were the main drivers of such a high growth of CRE prices recently. As for other fundamentals, they still demonstrate healthy state but it seems that majority of indicators have already shown their peaks of this cycle. NAREIT average same store NOI growth is still at relatively high levels but it has markedly decelerated from the peaks of the cycle, especially in Apartments and Retail segments where same-store NOI growth rates is at multi-year low levels. We don't exclude reacceleration of NOI growth in the foreseeable future but it will be difficult without the implementation of the promised reforms given the late cycle of the economy, decelerating rent growth, job market near full employment and occupancy rates at multi-year highs. But we don't expect as serious losses as in the last loan cycle because LTV rates are markedly lower and average REIT's interest coverage ratio is well above than it was in 2000-2010 years. Despite a majority of banks continue to express optimism on CRE sector, some of them indicated a more cautious approach to CRE lending during 3Q17 earnings.

Mortgage

Mortgage loans growth rate decelerated to 4.1% yoy (as of November 22) vs +6% yoy 1 year ago, but it remains relatively stable since March 2017, hovering around 4%. It remained resistant even to significant volatility in mortgage rates during this year.

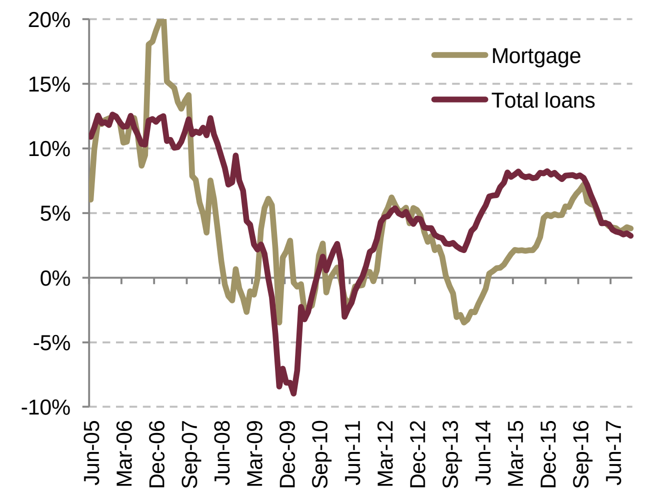
30-yr mortgage rate declined to the lowest level since November 2016 in early September, decreasing from February high of 4.19% to 3.67% in September, but it increased after that by 16 bps in absolute terms to 3.82% as the end of November. It is still -37 bps YTD but it remains significantly higher than average rate of the last year. Growth of mortgage loans also remains immune to eased lending standards. The October Senior Loan Officer Survey indicated that lending standards for all surveyed categories of mortgage lending either eased or remained basically unchanged over the past three months. "Meanwhile, a moderate net share of banks reported weaker demand for all categories of RRE loans, and a modest net share of banks reported weaker demand for revolving home equity lines of credit". Specifically, banks eased standards for GSE-eligible loans or for jumbo qualified loans while standards for other categories were basically unchanged.

Chart 14. Mortgage. 30yr Fixed Mrtg vs 10yr Tr yield, %



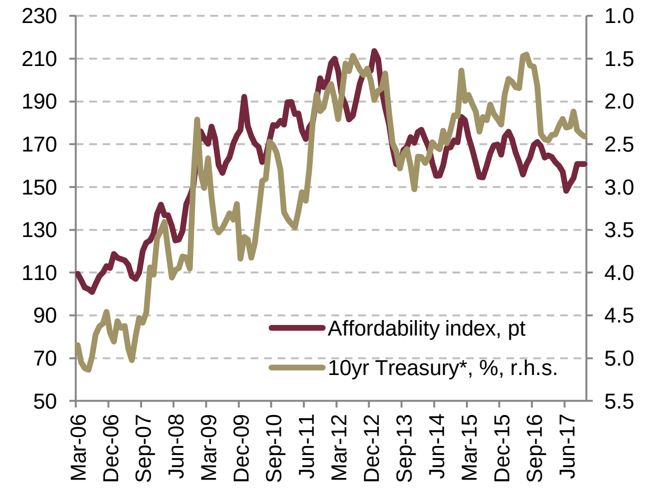
Source: Bloomberg

Chart 15. Loan Growth. Mrtg vs Total Loans, YoY, %



Source: Bloomberg

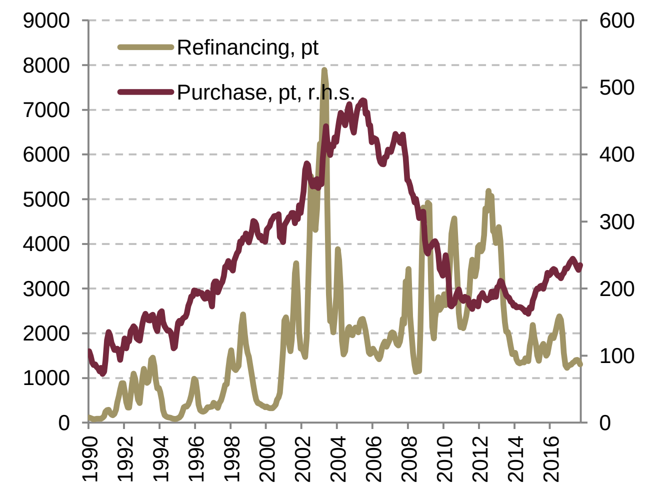
Chart 16. Mortgage. Aff. Index vs 10yr Treasury yield



*reversed order

Source: Bloomberg

Chart 17. Mortgage. MBA Applications Indexes



Source: Bloomberg

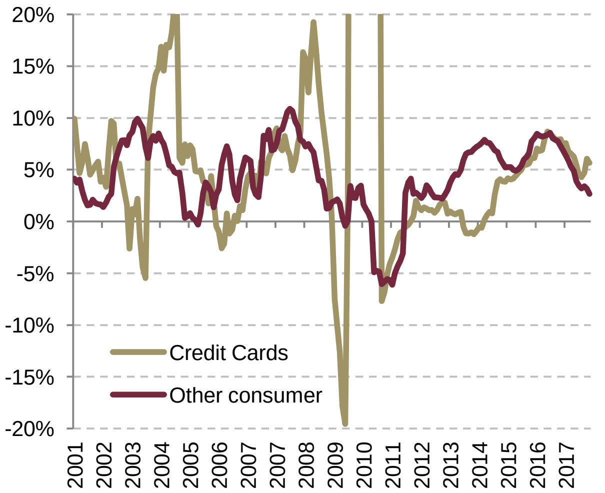
Housing market indicators were relatively strong in November, showing positive surprises for most indicators. Overall, fundamentals of housing market remain solid and we don't see significant risks in this segment at the moment (from quality of the loan portfolio point of view) but there are some imbalances in this segment indicating late cycle. Risks are still low, but the situation might change in future in case of a slowdown in the economy along with a significant growth of interest rates. The key problem for banks is relatively weak mortgage revenues because of tightening mortgage spreads and lower refinancing activity due to rising long end. The other risk for mortgage market is tax reform which proposals could negatively impact on some housing markets but this impact will be restricted. In turn, mortgage indicators remained weak vs 1 yr ago despite significant decline of long-end from its highs of the last year. Mortgage applications ticked up recently but it is still significantly below the pre-election levels because of substantial decline in refinancing applications. According to MBA's November 2017 forecasts, total mortgage originations will decrease by 17.6% yoy in 2017, driven by 40% yoy decline of refinancing volumes while purchase originations should increase by 5.5% yoy (marked decrease from previous estimates). The forecast also implies a further decline of total mortgage origination in 2018, by 5.4% yoy.

Recent hurricanes Harvey and Irma continue to influence both housing and mortgage data. It is not a surprise, taking into account that these hurricanes hit one of the biggest and one of the fastest growing areas of the U.S. real estate market. But currently, we see positive surprises on majority of housing macro indicators due to relatively weak figures in the previous months. Construction spending increased by +0.3% MoM in September vs consensus of -0.2% MoM, the second consecutive month of positive growth, but August figure was revised down from +0.5% MoM to +0.1% MoM. Housing starts increased to 1.29 mln units in October from revised up September's figure of 1.135 mln vs expectations of 1.19 mln units. Building permits also grew to 1.3 mln units in October from revised up September's figure of 1.23 mln vs expectations of 1.25 mln units. In turn, NAHB housing index increased by 3 pts in November to 70 pts vs expectations of 67 pts. It was the second consecutive month of growth and index almost returned to its 18-year highs of 72 pts. Existing home sales also increased in October to 5.49 mln from revised down September's figure of 5.37 mln vs estimates of 5.4 mln. New home sales in October increased to 685K from September revised down figure of 645K, significantly beating consensus of 628K. Housing prices continue to grow, but the growth isn't strong. S&P CoreLogic index increased by 0.5% MoM September vs expectations of +0.3%, mainly flat growth rate vs previous months growth rates.

Consumer

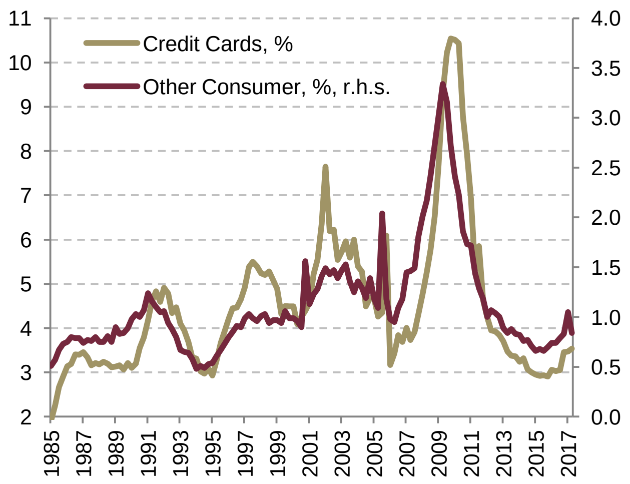
According to Fed H8 data, consumer loan growth yoy rate is currently +5.4% (through November 22th) vs 7.8% yoy 1 year ago. Consumer credit growth significantly accelerated during last month due to speed up of credit card loan growth which is currently at 7.5% yoy vs +7.7% 1 year ago and +4.7% yoy in yearly October 2017. Net change of consumer credit in September was +$20.83 bn vs consensus of +$17.5 bn and August figure of +$13.1 bn. It is the largest gain in 11 months. However, loan growth of other consumer (not credit cards) remains anemic at +3% yoy vs +7.9% yoy 1 yr ago. Anyway, consumer loan growth remains relatively weak despite strong job market and low levels of debt-service-ratios. The one reason is tightening loan standards because of accelerated loan growth in some consumer areas during the last credit cycle.

Chart 18. Consumer. Loan Growth Rates, YoY, %



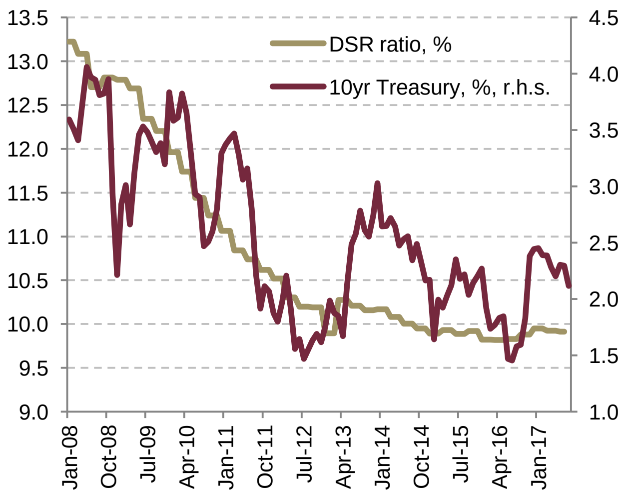
Source: Bloomberg

Chart 19. Consumer. NCOs Ratios, %



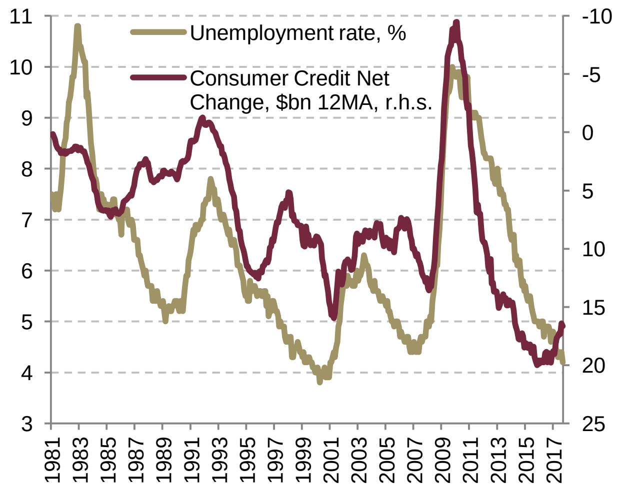
Source: Bloomberg

Chart 20. Debt Service Ratio vs 10yr Treasury Yield, %



Source: Bloomberg

Chart 21. Consumer. Loan Growth Rate, YoY, %



Source: Bloomberg

The October Senior Loan Officer Survey indicated that lending standards for consumer loans were tightened in the last three months. Specifically, standards were tightened in Credit Cards and Auto loans while standards for other consumer loans were basically unchanged. “Also, a moderate net share of banks reported an increased willingness to make consumer installment loans”. “Regarding terms on credit card loans, modest net shares of banks reportedly increased their minimum required credit scores and decreased the extent to which loans are granted to some customers that do not meet credit scoring thresholds”. The other terms were basically unchanged. As for auto loans, banks tightened majority of surveyed terms. However, banks indicated that demand remained basically unchanged.

The October survey included several special questions regarding reasons for changing standards and demand expectations in auto and credit card segments. “Major shares of banks reported that a less favorable or more uncertain economic outlook, a deterioration or expected deterioration in the quality of their existing loan portfolio, and a reduced tolerance for risk were important reasons for tightening their standards or terms on credit card and auto loans to prime and subprime borrowers”. Banks also indicated that less certain expectations regarding collateral value is important reason for tightening standards in auto segment. Answering special demand questions, “Major shares of banks reported that an increase in the general level of interest rates and that customers’ borrowing had shifted from their bank to other bank or nonbank sources were important reasons for weaker demand for auto loans from prime borrowers this year”.

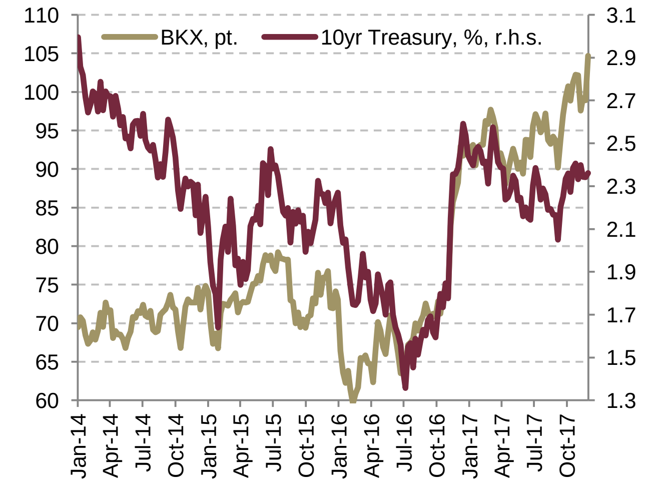
Most measures of consumer activity continue to demonstrate strength. Conference Board Consumer Confidence increased by 3.6 pts in November to 129.5 points (vs expectations of 124 pts), the highest level in 17 yrs. However, consumer sentiment index of Michigan University (preliminary) was worse than expectations, 97.8 pts in November vs expectations of 100.8 pts and September’s figure of 100.7 pts. Sentiment index of Michigan University remains near its post-housing bubble period peak. Consumer’s sentiment continues to be driven by good income prospects and strong labor market.

Employment data was mixed but we perceive October employment report as positive after clearly negative reading in the previous month because of the hurricanes impact. Nonfarm payrolls increased by 235k in October, missing estimates of +302k. September’s figure was revised up from -40K to +15K. Unemployment ratio decreased from 4.2% in September to 4.1% in October. Underemployment rate also decreased from 8.3% to 7.9%. The key disappointment of the employment report was average hourly earnings which were flat MoM (after significant growth in the previous month) vs consensus of +0.2% MoM. Initial Jobless Claims slightly increased in November (avg of 242K vs 233K in October), but the indicator continues to be relatively stable and near more than 40-yr lows. Overall, financial health of US consumer remains strong. But banks continue to be cautious and it continues to tighten credit standards, especially in risky areas such as auto lending which significantly outgrew majority of other consumer segments during the last credit cycle. Taking into account ongoing rate hikes cycle, financial pressure on consumers will increase which suggests further deterioration in the quality of the loan portfolio. Moreover, banks have built card credit reserves recently. But we don’t think that it could be a significant threat for credit quality of the loan portfolio, at least, in the near future. Moreover, the situation should improve after approval of the tax reform following which we see acceleration of US economy.

Interest Rates

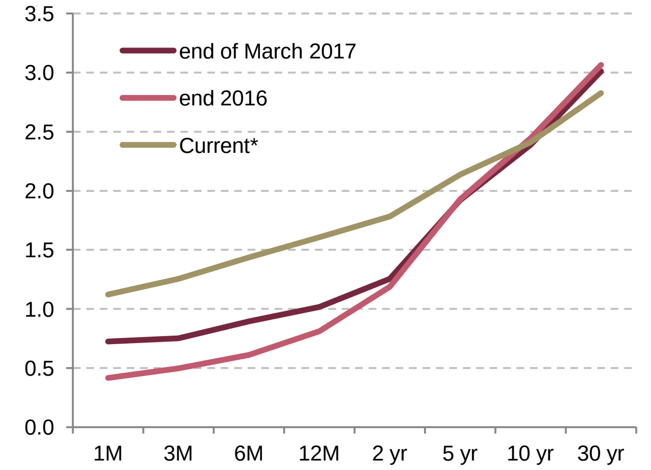
As was widely expected, the FOMC left the Fed funds rate unchanged at the November meeting, which was held on November 1. Overall, there were almost no changes in the statement. But taking into account recent macro data and the minutes from the November FOMC meeting, there is little doubt that FOMC will not hike rate at the December meeting (December 13). Currently, the market estimates the probability of the event at 98.3% vs around 20% as start of September. Despite the majority of the FOMC members consider current low inflation as temporary event, the minutes contained quite a long discussion about low inflation. In turn, inflation estimates were slightly revised down and it was noted that core inflation remained soft. Also, the wording about growth of the economy was changed to “solid” from “moderate”. Overall, the FOMC meeting announcements are quite positive for operating results of US banks as rates will probably continue to rise but it seems that it has already been largely priced in.

Chart 22. BKX Index vs 10yr Treasury Yield



Source: Bloomberg

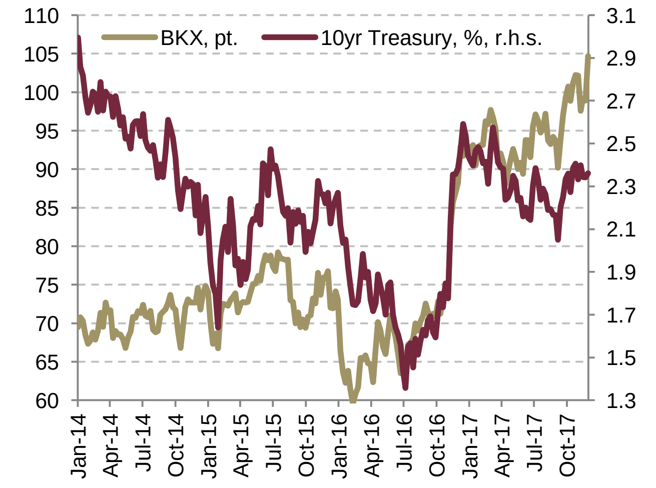
Chart 23. US Yield Curves, %



*As of 31 of October 2017

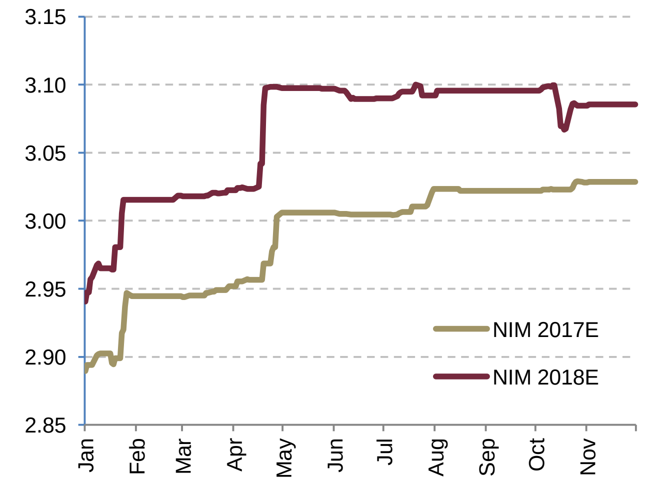
Source: Bloomberg

Chart 24. Corporate Yield Indices, 10yr



Source: Bloomberg

Chart 25. Median NIM of BKX index, %



Source: Bloomberg

Moreover, deposit beta has begun to grow fast enough recently. Currently, it is already around 40% at some banks. Of course, average beta is still significantly below levels of the previous cycles, but it has already started negatively impact on NIM growth. The other problem is flattening yield curve that fully complies with the previous Fed tightening cycles when the yield curve flattened during the rate hike cycle. 10yr-2yr spread continues to go down and currently it is near the lowest level since 2007. The yield curve is far from being inverted (a good predictor of an upcoming recession) but current level of spreads points to the late cycle along with rising labor costs, rising FF rate and declining profit margins. The key question is how many times the rate will be raised in 2018. The dot-plot still implies another 3 rate hikes in the next year. Obviously, it will depend on the upcoming macro data, especially inflation figures. The latter could accelerate in the near future due to tax cuts and the subsequent speed-up of the economy. Taking into account all of the above, we don't expect that rate hikes will continue to be as strong driver of banks' quotes as it was earlier in this cycle.

The other important event of the last month was appointment of Jeremy Powell to the head of the Fed. The market didn't react to this news as it was widely expected appointment. Moreover, it should not change the Fed's monetary policy considerably. Yellen's term expires only in the early February 2018, so the official changing will not happen earlier.

Treasury yields continued to grow in November after a small increase in October. 1M yield went up by 15.2 bps MoM to 1.12% while 3M yield came up by 12.5 bps MoM to 1.26%. Long end also showed growth, except for 30-yr yield: 2yr yield increased by 18.2 bps MoM, 5yr yield went up by 12.1 bps and 10yr yield grew by 3.0 bps.

Short end of the curve continues its growth after significant upturn in two previous months. Currently, it is markedly higher than the levels of the beginning of the year, while the long end of the curve remains significantly below than the end-February levels, and they also remained significantly lower end of 2016 yr levels. So, the yield curve continues to flatten. Currently, treasury spread (5yr-3Mo) is 0.88% or -0.4 bps MoM in November vs 1.33% of 5yr-3Mo treasury spread in the end of February. Steeper yield curve could be a positive driver for banks' profits, but we don't expect that the yield curve will become much steeper from current levels given the probable pace of the Fed rate hikes in the future.

According to Bankrate data, loan yields increased in November following the growth of the yield curve, except for mortgage rates. 30yr mortgage rate went down by 1 bps MoM to 3.87%. Auto loans rate (New loans, 60 mnth) increased by 16 bps to 3.48% in November after decline of 9 bps MoM in October. Deposit rates remained mostly unchanged in November. Only 5yr CDs grew in November, increasing by 2 bps MoM to 1.49%. 3Q17 earnings season showed that deposit betas continued to go up, currently being around 30% and we expect that deposit beta will continue to grow further decreasing sensitivity of bank's balance sheets to future rate hikes. Typically, NIM of US banks lagged the Fed rate hikes in the previous cycles, but the current situation in the industry is different due to very low beta. But 3Q17 earnings season showed that beta is gradually approaching the levels of previous cycles.

Europe

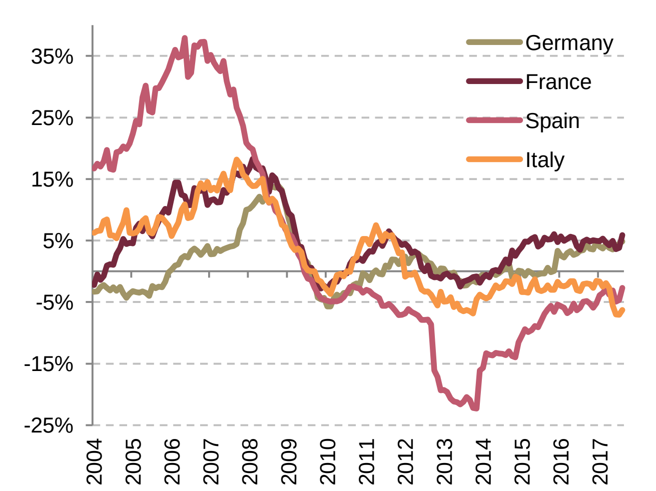
Corporate

According to October 2017 euro area bank lending survey, net demand for loans to enterprises continued to increase in 3Q17, but unadjusted EOP corporate loans decreased by 0.15% yoy. Adjusted loans increased by 2.4% yoy, 25th consecutive month of positive yearly growth. Despite relatively good adjusted figures, we still think that corporate loan growth remains weak given strong recent macro data with moderate acceleration of EU GDP growth this year. Loan dynamics was relatively uniform among major European countries. On year over year basis, loan growth accelerated in all major European countries but loan growth in EU still remains significantly different across the board. We see very healthy corporate loan growth in Germany and France while Italian and Spanish corporate loan growth is still deeply negative.

In line with October BLS, credit standards for corporate loans were broadly unchanged in 3Q17. But the net percentage remained considerably below the historical average since 2003, although it was above the expectation in the previous round (banks had expected slight easing). Bank's standards were broadly unchanged for small and medium-sized corporations, but eased on loans to large firms. "Across the large euro area countries, credit standards eased in Germany, tightened in Spain and remained unchanged in France and Italy". The key driver of easing standards remains competitive pressure, while effect of cost of funding and BS constraints was not decisive. Banks continue to point on narrowing margins on average loans as one of key drivers of easing standards. Net demand for loans to enterprises continued to increase in 3Q17, in line with expectations of the previous BLS. "Across the large euro area countries, net demand for loans to enterprises increased in Germany, Spain, France and Italy". The key drivers of demand growth were increase in CAPEX and ongoing low level of interest rates.

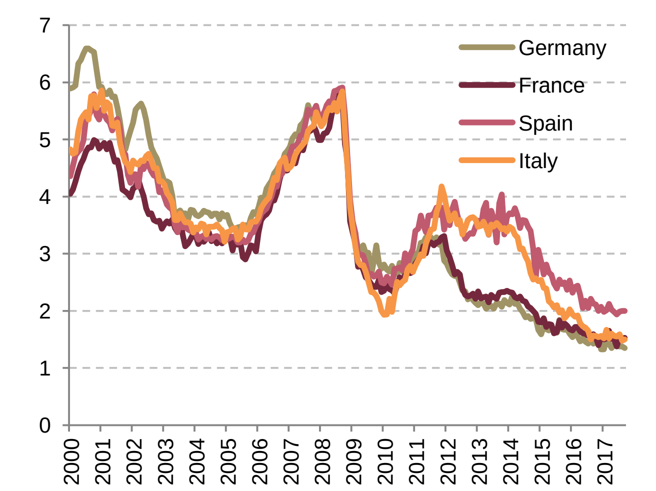
Germany outstanding corporate loans increased by 4.5% yoy and +0.4% MoM in September vs 4.8% yoy in February 2017 and +3.3% yoy in September 2016. French corporate loans outstanding added +3.8% YoY +0.2% MoM vs +3.7% yoy in December 2016 and +3.5% in September 2016. As for Spain and Italy, its outstanding corporate loans continue to decrease, -4.7% yoy and -6.9% yoy in September 2017, respectively. Moreover, the rate of fall of corporate loans both in Spain and Italy significantly accelerated in the recent months.

Chart 26. EU Corporate Loan Growth, YoY



Source: Bloomberg

Chart 27. EU Corporate Loan Rates, New Loans, %



Source: Bloomberg

European corporate rates still demonstrate weak dynamics. However, it has been appearing more and more encouraging signs recently. Average EU corporate loan rates (all maturities, new business lending) increased by 9 bps MoM in August, it is the second consecutive month of growth. The yield already grew by 16 bps from its June's low of

1.98%. Moreover, it added +3 bps yoy, the first time of positive yoy growth in more than 3.5 years. In turn, average rate of outstanding loans continues to go down, -1.6 bps MoM and -20 bps YoY in August. Back book yields of EU banks were non-stop decreasing since April 2014 but it has also decelerated recently from rate of decline of -22.1 bps yoy in April 2017 to the current level. The most substantial increase was showed in France, where August rates on new corporate loans increased by 16 bps to 1.54%. Spanish and Italian rates on new corporate loans also went up in August but only by 5 bps MoM. Germany rates decreased by 1 bps in August to 1.38% after -2 bps MoM decline in July. In fairness, spreads between new and outstanding rates continue to shrink but they still far from the positive territory for all major European countries except for Spain where it is currently at +3 bps. We do not expect significant changes in the situation until ECB will not start to hike rates as short-term rates still remain in deeply negative territory. But, it seems that market has already started to buy on a future rate hikes although, from our point of view, it will happen not earlier than in 1.5 years.

Consumer

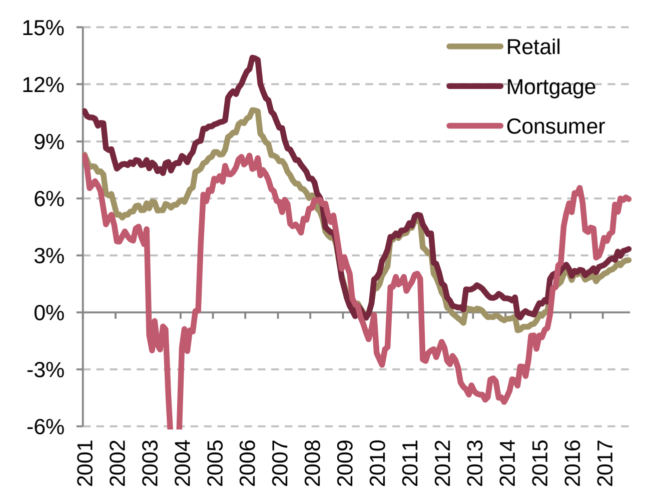
EU loans to households increased by 2.7% yoy in September (vs +1.9% in September 2016) that it is markedly higher than average level of the last year, +1.7% yoy. Consumer loans continue gaining momentum but the rate of growth of the loan portfolio continues to differ widely across countries, German household loans increased by 4.0% yoy in September, French retail lending added 5.3% yoy in September (significant acceleration vs January 2017 growth of 4% yoy), while household loans in Spain decreased by 1.6% yoy in September. Italian consumer loans added +0.8% yoy in September (vs +2.1% yoy growth 1 year ago). All major European countries except for Italy markedly accelerated consumer loan growth since the beginning of the year that fully consistent with the improvement of consumer financial health in Europe lately. Consumer confidence in Eurozone increased by 6.3 pts YTD, unemployment decreased by 0.6% YTD, retail sales continue to demonstrate robust growth.

Consumer lending (ex mortgage) still remains the key driver of EU household loan portfolio, adding 5.9% yoy or +0.4 MoM in September, vs +4.4% yoy in September 2016. EU mortgage loans increased by 3.3% yoy in September (vs 2.3% yoy one year ago) slightly accelerating from August yoy growth rate. And it broadly corresponds to what we saw in October 2017 lending survey from ECB, where it was noted ‘positive net percentage of banks continued to report an increase in demand for housing loans’. The most impressive growth in consumer segment continue to be demonstrated by Spain, where these loans rose by 13.8% yoy in September (vs +11.8% 1 year ago), while Spanish mortgage portfolio continues to stagnate, -2.7% yoy in September (vs -3.1% 1 year ago).

Average EU rates on new mortgage loans were flat MoM in September, after seven consecutive months of growth. The rate has already increased by 13 bps from the minimum level of January 2017. Moreover, on year-over-year basis, this yield also showed positive growth of 5 bps yoy. The key driver of mortgage rates was the long end of the yield curve. 10yr generic yield was approximately flat in November, decreasing by just -0.4 bps MoM. However, mortgage rates on new loans were relatively weak on month-over-month basis in all major European in September. German rate decreased by 1 bps MoM to 1.86% in September, French rate was flat MoM at 1.65%, Spanish rate crumbled by 9 bps MoM to 2.09% and Italian mortgage rate on new loans also decreased by 9 bps MoM to 1.97%. Unsurprisingly, we continue to see declining back book rates on year-over-basis, but average EU rate was flat on month-over-month basis in September. Thus, there is a deceleration of the rate of decline of back books recently due to steepening of the yield curve.

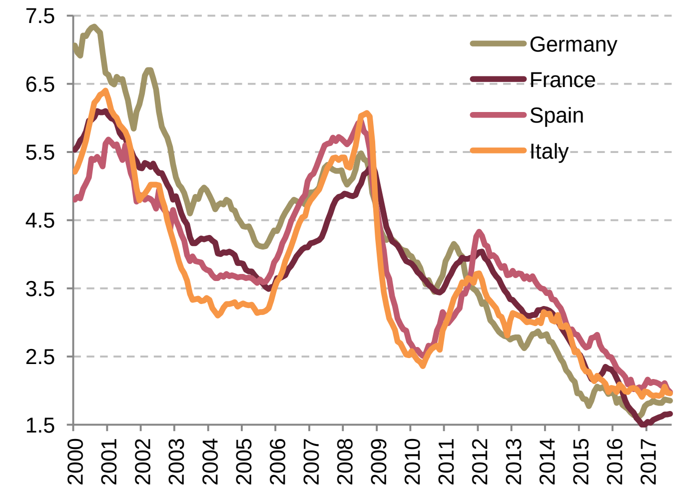
As for other consumer credits, EU new business rates tumbled by 19 bps MoM in September, after the significant growth of consumer yields in summer months. But current front book yield of consumer loans remains near its 5-year high, although it remains volatile. Front book consumer rates significantly decreased in all major European countries in August except for Spain, where it increased by 15 bps MoM to 7.82% in September. Italian consumer front book yield decreased by 16 bps MoM to 6.83%, French yield also decreased by 26 bps to 3.75% in September, while German rate went down by 21 bps to 5.65%.

Chart 28. EU Consumer Loan Growth, YoY



Source: Bloomberg

Chart 29. EU Mortgage Loan Rates, New Loans, %



Source: Bloomberg

Average European consumer deposits rate (with agreed maturity) for new deposits was flat on month-over-month basis in September at 0.28%. Cost of outstanding deposits (with agreed maturity) decreased by 1 bps MoM in August to 1.02% (-18 bps yoy) and it is not good for EU banks, as cost of deposits significantly decelerated its decline rate while yield of consumer loans continue to go down faster than cost of deposits.

According to the last BLS, "Credit standards for loans to households for house purchase eased further, with the change proving stronger than expected in the previous survey round. The net percentage is below the historical average since 2003. Banks eased their credit standards on housing loans across all the large euro area countries. Competitive pressure, banks' higher risk tolerance and lower risk perceptions contributed to the net easing of credit standards on housing loans, while the impact of cost of funds and balance sheet constraints was broadly neutral". Banks expect to continue ease credit standards further in 4Q17. As well as for loans to enterprises, the key driver of easing standards was narrowing margins on average loans. "Across all the large euro area countries, the general level of interest rates and housing market prospects continued to have a substantially positive effect on demand. Consumer confidence had a positive impact on demand in all the large countries except Italy, where it had a neutral effect".

Rates

EU rates were relatively flat in November because of dovish results of the October ECB meeting. As was widely expected, ECB announced that monthly asset purchases will be reduced from current €60 bn to €30 bn as of January 2018 but the overall tone of the meeting suggested that the ECB wouldn't hurry with the tightening of the monetary policy. The next ECB meeting will be held on 14 December, but we don't expect that we will hear any significant new details which force us to substantially change our current 2018/2019 rates forecast given still subdued inflation in Europe. ECB don't want to make any drastic steps and it prefers to tighten monetary policy gradually. At least, the ECB's wording is still cautious. There is a remark that ECB could continue net asset purchases at a monthly pace of €30 bn beyond September 2018 if necessary. Moreover, "If the outlook becomes less favorable, or if financial conditions become inconsistent with further progress towards a sustained adjustment in the path of inflation, the Governing Council stands ready to increase the APP in terms of size and/or duration". "The Eurosystem will reinvest the principal payments from maturing securities purchased under the APP for an extended period of time after the end of its net asset purchases, and in any case for as long as necessary". Key rates were remained unchanged and it will "remain at their present levels for an extended period of time, and well past the horizon of our net asset purchases".

In any case, further pace of monthly asset purchases will depend on the incoming information, including inflation and volatility in the exchange rate. Given the market expectations, the first rate hike will not happen earlier than in 1H2019, from our point of view, and negative deposit facility rate environment will persist at least until the middle of 2020. So, we still think that it is too early to buy banks because of possible rising rates in future taking into account very strong outperformance of European banks in the last year. Of course, fundamentals will continue gradually improve but the short end of the curve will not change significantly until the key policy rates will eventually start to grow; low rate environment will persist for several more years; growth of long end is largely already priced in, from our point of view; valuations don't look as reasonable as before; loan growth is still sluggish, especially in corporate segment while credit quality issues remains.

10yr EU generic yield was flat in November decreasing just by 0.4 bps MoM, after more dovish ECB meeting in September. It still remains markedly below of July's high, -24 bps, but it is materially higher than it was at the end of 2016, +16 bps YTD in absolute terms. However, the dynamics of the generic yields wasn't uniform during November. 1yr generic yield went down by 2 bps MoM, while 2yr yield increased by 6.6 bps MoM after almost the same decline in October. Overall, the middle of the curve increased, while the short end and the long one went down. Spread between 10yr yield and 1yr yield increased by 1.5 bps MoM. Spread between 5yr and 3M yields increased by 9 bps MoM to 0.43%.

Steeper yield curve is clearly positive driver for European banks but it is worth to note that the industry has been still operating in negative rate environment. Moreover, significant growth of the yield curve (first of all, the long end) from its last year lows hasn't transformed into growth of back book yields yet. But the recent dynamics of front book yields is encouraging. Higher rates remain the most important driver for European banks but, taking into account forward Euroribor curves, growth of short end of the curve is far from us, so marked acceleration of NIM growth is also not the near term event given reference rate of substantial share of EU loans is less than 1 year.

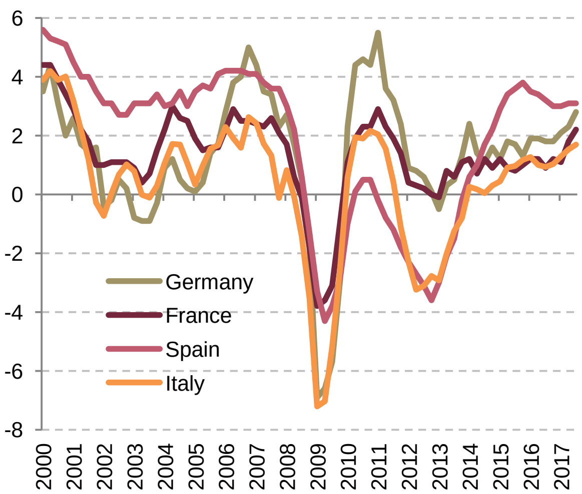
Macro indicators overview

Steady economic expansion in the euro area continues with GDP YoY growth higher than 2% and recent macro data indicates that it will remain solid in 2H2017. The second estimate of 3Q17 EU aggregate GDP growth was +0.6% QoQ and +2.5% YoY, in line with consensus and preliminary estimate. We don't exclude some deceleration of growth of EU economy because of euro strengthening, but it should still remain supportive for quotes of European banks in near years given the broad-based (the dispersion of growth rates of EU members is near the lowest level in 20 years) and self-sustained character of the current stage of recovery of the European economy. Eurozone GDP growth consensus was revised up by 10 bps for 2017 (to 2.2% yoy from 2.1% yoy 1 month ago), estimates of GDP 2018 was also revised up by 10 bps to 1.9% in the Bloomberg's November survey while consensus estimate of 2019 GDP growth was unchanged at 1.6%. GDP has already risen for 18 consecutive quarters and everything indicates that this growth will not end any time soon.

Composite PMI, which is well correlated with GDP growth, markedly increased in November after slight decrease in October but it remained at multi-year high. Preliminary composite index increased by 1.5 pts to 57.5 pts, well above consensus estimate of 56.0 pts. Manufacturing PMI also increased by 1.5 pts to 60.0 pts and it is currently at multi-year high, significantly beating consensus of 58.2 pts. Services PMI was also better than estimates, going up by 1.2 pts to 56.2 pts. PMI figures indicate that we will continue to see strong GDP growth further. It seems that strengthening euro has not had a significant negative impact on economic growth yet. PMI points at strong employment dynamics and business optimism figures. Economic sentiment in EU is at six-year high. A majority of business climate and business confidence indicators were relatively strong in November. Eurozone industrial production decreased by 0.6% MoM in September, matching the Bloomberg consensus expectations. IP demonstrated strong dynamics in the previous two months. In August, it added +1.4% significantly exceeded estimates of 0.6%. July's figure was revised up from +0.1% MoM to +0.3% MoM.

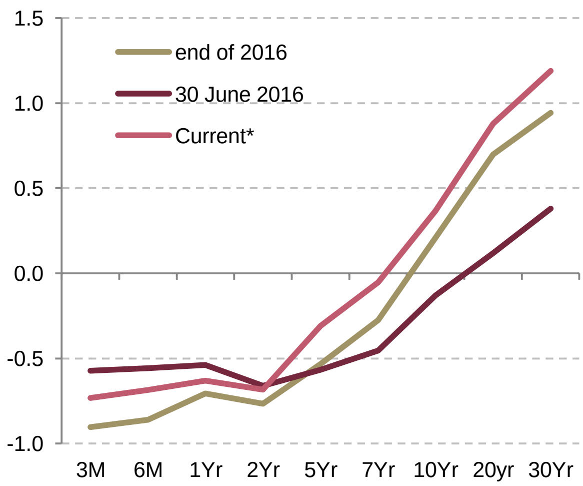
Consumer confidence continues to rally and it is currently at the highest level since 2001 year. Final November figure increased by 1.1 pts MoM to +0.1 pts. Current consumer confidence is by 6.3 pts higher than it was in the end of 2016. Growing consumer confidence is not surprising as the unemployment rate continues to decline even despite growth in labor force. October's unemployment rate decreased by 0.1% MoM to 8.8% beating consensus of 8.9%. Retail sales increased by 0.7% MoM in September, exceeding Bloomberg consensus of +0.6% MoM. August estimate was revised up significantly from -0.5% MoM to -0.1% MoM. Overall, outlook for EU consumer remains encouraging and we expect that consumer credit will continue to demonstrate robust growth further.

Chart 30. EU Countries Real GDP Growth, YoY, %



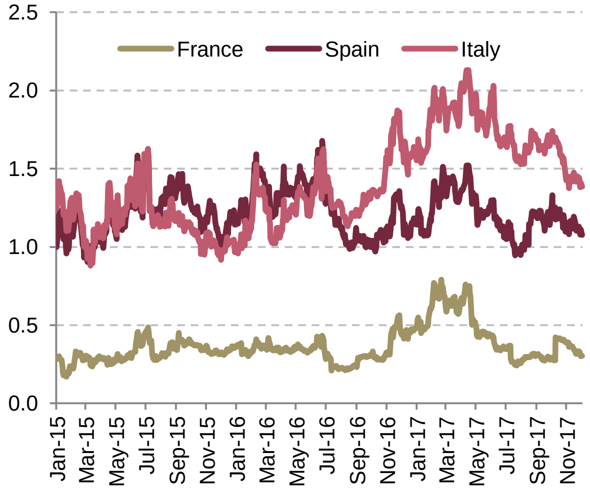
Source: Bloomberg

Chart 31. EU Yield Curves, %



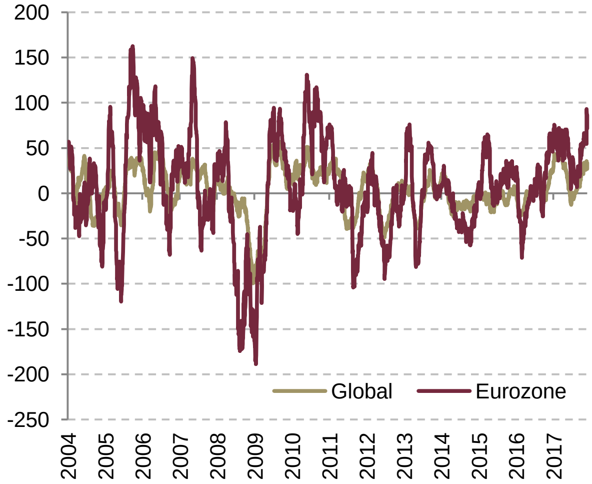
Source: Bloomberg

Chart 32. EU Countries Sov. Spreads vs Ger, 10Yr, %



Source: Bloomberg

Chart 33. Citi Economic Surprise Indexes, pt



Source: Bloomberg

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4. THEME OF THE MONTH

US Tax Reform

Tax reform was one of the main election promises of the president Trump. As we wrote one year ago, the reform shouldn't be implemented quickly because of a large number of procedural obstacles. Recently, the odds to complete tax reform in the near future have significantly increased due to approval of the bill in the House and successful talks in the Senate. The Budget Committee voted to send the Republican's tax plan to the Senate floor for a starting of the procedural discussion on November 28. It increased odds to enact the reform by the end of the year. But the probability of passing reform till the year end is still not 100%, from our point of view, as there is lack of time for it because of both the House and the Senate sessions will end in the middle of December while there are still too many disagreements between the Republicans and the Democrats. Moreover, it seems that the reform will finally be enacted with noticeable changes vs the initial proposal of the House Committee (from the 2nd of November). As for timeline, our current base case is that the legislation will be enacted by the end of the first quarter of 2018.

Banks positively reacted to the recent news as the tax reform is surely a good driver of EPS growth, even despite the proposed lowering the statutory federal corporate tax from 35% to 20% is markedly below than the initial Trump's promise of lowering it to 15%. BKX index added more than 5% during the last trading week of November. Technically, decreasing statutory tax rate is very positive for US banks, as most of the revenues they receive in the country and banks effective tax rate is around 30% on average, but future EPS boost is highly dependent on the final tax rate. If the statutory tax rate is decreased to 25% (not to 20% as in the House Committee proposal), median EPS benefit will be just around 10%. It is worth noting that the recent skyrocketing growth of banking quotes is also caused by the Powell's testimony where he said that the regulation was already tough enough and that banks weren't still too big to fail. This statement was interpreted as the sign of the further deregulation. The deregulation and the tax reform were positive risks for the banking quotes, so the current reaction of banking prices is understandable but the question is how justified was this movement as multipliers have already at rich levels while the uncertainty with reforms still remains. If there are some problems with the reform enactment and some changes compared to the House version of the bill, we could see a temporary correction in US banking stocks. But we consider this scenario as a buy opportunity because fundamentals of US banks still remain very strong.

The House Ways and Means Committee released its tax reform proposal on November 2. The key proposals of the bill are following:

- **Lowers the corporate tax rate to 20%.** From the current rate of 35%. It should take effect as early as in 2018 and should be permanent. It is the most valuable part of the bill for banks
- **Allows businesses to immediately write off the full cost of new equipment for 5 years.** Technically, accelerated depreciation has already actively used by US companies, but the initiative will positively impact on investments and CAPEX
- **Limit corporate net interest deductibility to 30% of EBITDA.** The key question is how intercompany loans will be considered.
- **Exempt international incomes from US taxes.** It was also proposed to tax deferred foreign income at a 14% for cash and 7% for reinvested incomes over

an 8-yr period.

- **Lower individual tax rates for low- and middle-income Americans to Zero, 12%, 25%, 35% and maintain 39.6% rate for high-incomes.**
- **Significantly increase the standard deductions for individuals.**
- **Eliminate special-interest deductions that increase rates and complicate Americans' taxes.**

Overall, the proposed bill roughly corresponded to what was proposed before the election by the House Republicans in mid-2016. But the estimated tax cuts are around $1.5 trln over next ten years and it is slightly higher than it was expected earlier.

The House Ways and Means Committee released its own version of the tax reform on November 9, which were approved by the Senate Finance Committee on November 16. Overall, both proposals largely look the same. But the devil is in the details. The estimated tax cuts of the Senate's bill are around $1.4 trln over ten years. The Senate's proposal implies lowering corporate tax rate from 35% to 20%, but it proposes to do it since 2019. The Senate's bill also imposes a more strict restriction on interest deductibility to 30% of "adjusted taxable income" vs 30% of EBITDA in the House bill. The Senate's bill also proposes to maintain the medical expense deductions vs elimination of it in the House bill. There is also a discussion about repeal of the Affordable Care Act mandate that implies widening of the revenue gap which should be covered, for example by higher corporate rates. Some senators propose to include in the bill a fiscal trigger which would lay claim to increase tax rate in case of miss of revenue targets. This option may negatively impact on long-term investments because of ongoing uncertainty about corporate taxes. Simply speaking, there are some disagreements between the Republicans and the Democrats which require a certain time to come to a consensus. And we are convinced that the final bill will be markedly different from the current proposals.

Of course, the tax reform should be very positive for US banks, as most of the revenues they receive in the country and their effective tax rate is 30% on average. The uncertainty around the final version of tax reform is still relatively high (even timing, at least timing of effective date of lowered tax rate), but banking quotes has already reacted positively. It is understandable as banks should also benefit from second-order effects of accelerating economy, elimination of uncertainty. Deregulation and further growth of rates also positively impact on operating results of US banks. The key question is how justified multipliers are. In absolute terms, banking multipliers look rich. The key beneficiaries of the tax reform should be consumer finance companies (COF, SYF, DFS) with the highest effective tax rate, but we continue to overweight money-centers (JPM, BAC, C) which should significantly benefit not only from tax reform but also from deregulation, rising rates and deployment of the excess capital.

APPENDIX

Table 1. US Banks: Valuations

Company	Ticker	Price, $ (30/11/17)	Target price, $	Upside	52-week price, $ High	52-week price, $ Low	RSI	MCap, $ bn.	Dividend yield 2017E	Dividend yield 2018E	Dividend yield 2019E	Price/Earnings 2017E	Price/Earnings 2018E	Price/Earnings 2019E	Price to book	Price to tang. book	ROE, % 2017E	ROE, % 2018E	ROE, % 2019E	TCE ratio, %	CET1 ratio, %
American Express	AXP	97.7	96.0	-1.8%	98.5	71.4	72.1	84.8	1.4%	1.5%	1.6%	16.7	15.1	13.7	4.0	N. A.	25.5	26.5	27.8	10.8	12.3
JP Morgan Chase	JPM	104.5	101.3	-3.1%	106.7	80.7	73.5	362.7	2.0%	2.3%	2.6%	15.2	13.6	12.3	1.6	2.0	10.5	11.2	11.5	7.4	12.5
PNC Financial	PNC	140.6	141.4	0.6%	143.1	110.7	72.4	66.9	1.9%	2.3%	2.5%	16.7	15.0	13.8	1.6	2.0	9.5	10.1	10.6	9.1	10.6
Bank of America	BAC	28.2	28.4	0.9%	28.7	21.0	68.9	293.8	1.4%	2.0%	2.7%	15.5	13.0	11.5	1.2	1.6	7.9	8.8	9.3	8.0	12.1
Citigroup	C	75.5	77.5	2.7%	76.9	55.2	67.2	199.6	1.3%	1.9%	2.4%	14.4	12.8	11.1	1.0	1.1	6.8	7.2	7.8	10.1	14.9
BB&T Corp	BBT	49.4	49.0	-0.8%	50.1	41.2	67.9	39.0	2.5%	2.8%	3.1%	15.9	14.4	13.6	1.5	2.4	9.2	9.6	9.7	7.8	10.2
Goldman Sachs	GS	247.6	249.9	0.9%	255.1	209.7	65.5	97.0	1.2%	1.3%	1.4%	12.9	12.1	10.9	1.3	1.3	10.3	10.1	10.9	8.4	13.1
SunTrust Banks	STI	61.6	63.9	3.7%	62.9	51.8	69.3	29.3	2.2%	2.7%	3.0%	15.2	13.9	12.9	1.3	2.0	8.6	9.0	9.2	7.3	9.6
Bank of NY Mellon	BK	54.7	56.8	3.7%	55.3	43.9	73.5	56.1	1.6%	1.9%	2.1%	15.4	14.1	12.9	1.5	3.5	10.1	10.4	10.9	4.6	9.7
Comerica	CMA	83.3	81.3	-2.4%	85.3	64.0	69.8	14.5	1.3%	1.6%	1.8%	17.6	15.4	14.0	1.8	2.0	10.6	11.4	11.8	9.9	11.1
Citizens Financial	CFG	40.7	40.9	0.4%	41.8	31.5	72.7	20.0	1.6%	2.2%	2.5%	15.8	14.4	13.0	1.0	1.6	6.6	6.9	7.2	8.8	11.2
Regions Financial	RF	16.6	16.1	-2.9%	16.9	13.0	71.0	19.2	1.9%	2.4%	2.7%	16.6	14.5	13.2	1.2	1.8	7.4	8.1	8.6	8.7	11.1
Discover Financial	DFS	70.6	73.9	4.7%	74.3	57.5	74.3	25.7	1.8%	2.0%	2.2%	11.9	10.7	9.6	2.4	2.5	20.4	21.3	22.2	11.2	13.2
M&T Bank	MTB	169.0	164.3	-2.8%	173.7	141.2	65.6	25.4	1.8%	1.9%	2.1%	18.4	16.9	15.9	1.7	2.5	9.2	9.6	9.9	8.9	11.0
Fifth Third Bancorp	FITB	30.5	28.9	-5.2%	31.1	23.3	73.3	21.5	2.0%	2.3%	2.5%	16.8	14.9	13.8	1.4	1.7	10.1	9.4	9.7	8.9	10.4
Huntington Bancorp	HBAN	14.4	15.2	5.2%	14.8	12.2	67.8	15.6	2.4%	3.2%	3.4%	14.7	13.6	12.6	1.6	2.1	10.3	11.3	11.8	7.0	9.6
Northern Trust	NTRS	97.8	99.3	1.6%	99.3	81.8	70.0	22.2	1.6%	1.8%	2.0%	20.4	18.2	16.8	2.3	2.5	12.0	13.1	13.8	7.0	12.4
People's United	PBCT	19.0	18.3	-3.6%	20.1	16.0	63.4	6.6	3.6%	3.6%	3.7%	19.5	16.8	15.8	1.2	2.2	6.0	6.7	7.0	7.1	9.9
Synchrony Financial	SYF	35.9	38.1	6.0%	38.1	26.0	76.3	28.1	1.6%	1.8%	2.0%	13.8	11.4	9.8	2.0	2.2	14.5	16.9	18.8	14.2	17.2
KeyCorp	KEY	19.0	20.5	8.0%	19.5	16.3	63.4	20.4	2.0%	2.6%	3.0%	14.0	12.5	11.6	1.4	1.7	10.2	10.8	11.4	9.3	9.5
State Street Corp	STT	95.4	103.9	9.0%	100.0	75.1	60.7	35.4	1.7%	1.8%	2.0%	15.2	13.7	12.7	1.8	3.1	12.7	13.0	13.5	4.4	11.6
US Bancorp	USB	55.2	55.9	1.4%	56.6	49.5	70.1	91.5	2.1%	2.3%	2.5%	16.1	14.8	13.9	2.1	3.0	13.3	13.3	13.5	7.2	9.4
Zions Bancorp	ZION	49.6	50.7	2.3%	50.5	38.4	70.1	9.9	0.9%	1.9%	2.2%	18.0	15.7	14.5	1.4	1.6	8.2	8.9	9.2	9.5	12.1
Morgan Stanley	MS	51.6	52.5	1.6%	52.6	40.1	69.2	93.3	1.7%	2.1%	2.7%	14.3	12.8	11.6	1.3	1.5	9.3	9.8	10.5	7.4	16.9
Capital One Financial	COF	92.0	96.8	5.2%	96.9	76.1	64.6	44.6	1.7%	1.8%	2.0%	12.0	10.7	9.6	1.0	1.4	8.2	8.5	8.9	8.2	10.1
Wells Fargo	WFC	56.5	58.4	3.4%	60.0	49.3	63.6	278.1	2.7%	2.9%	3.1%	14.2	13.1	11.9	1.5	1.8	11.1	11.4	11.7	7.7	11.1
First Republic Banks	FRC	95.5	102.5	7.3%	105.4	82.5	53.7	15.3	0.7%	0.8%	0.8%	21.9	19.0	17.1	2.3	2.5	11.2	11.6	11.9	7.5	10.8
NY Commercial Bancshares	NYCB	13.3	12.8	-4.1%	17.7	11.7	63.4	6.5	5.1%	5.1%	5.1%	18.6	17.6	18.0	1.0	1.7	5.7	5.6	5.6	7.9	10.6
SVB Financial	SIVB	227.6	227.9	0.1%	233.5	158.2	77.0	12.0	0.0%	0.0%	N. A.	23.9	19.6	16.9	3.0	3.0	12.5	12.9	14.2	8.2	12.8
Signature Bank	SBNY	137.3	147.6	7.5%	164.2	116.7	65.2	7.5	N. A.	N. A.	N. A.	20.0	14.6	13.5	1.9	1.9	10.2	11.9	11.6	9.3	11.9
East West Bancorp	EWBC	61.5	65.0	5.6%	62.7	47.9	68.5	8.9	1.3%	1.4%	1.6%	17.7	16.1	14.5	2.4	2.7	14.5	13.6	13.9	8.5	10.9
Synovus Financial	SNV	49.6	48.5	-2.3%	50.5	38.0	72.3	5.9	1.2%	1.4%	1.6%	20.3	17.2	16.0	2.1	2.1	10.4	11.5	11.5	9.1	10.0
First Horizon National	FHN	19.4	21.0	8.2%	20.8	15.8	61.0	4.5	1.9%	2.1%	2.5%	17.5	15.1	13.3	1.8	2.1	10.7	9.7	10.8	7.4	9.9
BOK Financial	BOKF	89.0	89.8	0.9%	91.5	73.5	62.9	5.8	2.0%	2.0%	2.1%	16.7	16.3	15.5	1.9	2.2	10.1	9.6	9.5	8.6	11.2
Median				**1.5%**			**69.1**		**1.7%**	**2.0%**	**2.5%**	**16.4**	**14.6**	**13.4**	**1.6**	**2.0**	**10.2**	**10.3**	**10.9**	**8.3**	**11.1**

Source: Bloomberg

ARBAT CAPITAL

APPENDIX

Table 2. EU Banks: Valuations

Company	Ticker	Currency	Price* (30/11/17)	Target price*	Upside	52-week price*		RSI	MCap, € bn.	Dividend yield			Price/Earnings			Price to book	Price to tang. book	ROE, %			TCE ratio, %	CET1 ratio, %
						High	Low			2017E	2018E	2019E	2017E	2018E	2019E			2017E	2018E	2019E		
Erste Group	EBS AV	EUR	36.7	39.2	6.9%	38.6	25.1	50.3	15.1	3.1%	3.6%	4.5%	12.8	12.1	11.3	1.2	1.3	9.9	9.8	10.0	5.1	13.1
Raiffeisen Bank	RBI AV	EUR	29.8	28.6	-3.9%	31.0	16.7	52.2	8.2	2.2%	3.1%	4.2%	10.6	9.6	8.7	1.0	1.1	10.5	9.4	9.5	7.2	13.9
KBC Groep	KBC BB	EUR	68.7	73.8	7.3%	73.0	56.0	41.8	29.3	4.5%	4.6%	5.3%	12.1	12.8	12.5	1.7	1.8	15.2	13.5	12.9	5.5	16.2
Komercni Banka	KOMB CK	CZK	899.0	1021.6	13.6%	1013.0	840.2	28.5	6.9	4.8%	4.7%	5.1%	14.2	14.0	13.5	1.8	N. A.	13.2	12.2	12.3	10.3	16.2
Jyske Bank	JYSK DC	DKK	337.8	360.7	6.8%	399.8	300.0	43.5	5.0	3.2%	2.9%	3.5%	11.7	11.8	10.6	0.9	0.9	9.6	8.3	8.6	5.3	16.5
SydBank	SYDB DC	DKK	244.5	263.5	7.8%	266.0	203.3	46.1	2.5	4.7%	4.5%	4.8%	12.1	12.1	11.0	1.4	1.4	13.1	11.8	12.4	7.8	16.1
Danske Bank	DANSKE DC	DKK	233.6	275.4	17.9%	259.5	202.4	40.6	32.1	4.2%	4.5%	4.8%	12.2	11.8	11.0	1.4	1.5	12.6	12.5	12.9	4.2	16.3
BNP Paribas	BNP FP	EUR	63.6	71.0	11.7%	69.2	53.8	42.4	81.9	4.7%	4.8%	5.3%	10.9	10.3	9.5	0.9	1.0	8.5	8.2	8.5	3.8	11.6
Natixis	KN FP	EUR	6.8	7.1	3.6%	7.0	4.8	60.1	19.3	5.5%	5.8%	6.2%	13.4	12.1	11.0	1.1	N. A.	7.9	9.0	9.7	2.7	10.8
Societe Generale	GLE FP	EUR	42.3	49.4	16.8%	52.3	39.5	26.4	40.1	5.1%	5.6%	6.0%	11.1	10.0	9.3	0.6	N. A.	6.2	7.1	7.5	4.0	11.8
Credit Agricole	ACA FO	EUR	14.2	15.7	11.0%	15.7	10.4	41.6	42.3	4.6%	4.8%	5.3%	12.6	11.4	10.3	0.7	N. A.	6.9	6.9	8.2	2.6	12.1
CYBG	CYBG LN	GBp	313.8	273.2	-12.9%	321.6	257.1	52.6	2.6	0.0%	0.1%	0.1%	14.1	12.6	10.7	0.8	0.9	6.0	7.3	7.9	7.1	12.4
HSBC	HSBA LN	GBp	734.0	756.2	3.0%	772.0	618.0	47.0	170.3	0.1%	0.1%	0.1%	12.2	11.3	10.4	1.0	N. A.	7.8	8.3	8.6	6.5	13.6
Royal Bank of Scotland	RBS LN	GBp	276.6	285.8	3.3%	290.5	191.0	53.6	33.0	0.0%	0.0%	0.1%	11.7	10.4	9.1	0.7	0.8	7.1	7.4	7.8	5.3	13.4
Barclays	BARC LN	GBp	193.5	209.4	8.2%	244.4	177.3	63.4	38.6	0.0%	0.0%	0.0%	11.9	9.0	8.5	0.6	0.7	2.5	6.0	6.7	4.2	12.4
Standard Charted	STAN LN	GBp	738.4	706.2	-4.4%	860.0	634.1	50.4	31.1	0.0%	0.0%	0.1%	16.2	11.4	9.3	0.6	0.7	3.8	5.0	6.1	6.8	13.6
Lloyds	LLOY LN	GBp	66.0	71.7	8.7%	73.5	56.5	47.1	52.6	0.1%	0.1%	0.1%	8.9	9.1	9.1	1.1	1.2	13.1	12.3	11.8	4.8	13.6
Commerzbank	CBK GY	EUR	12.2	11.2	-7.8%	12.5	6.4	58.0	13.9	0.0%	0.6%	2.2%	27.0	15.2	10.5	0.5	0.6	1.0	3.0	4.5	5.4	13.9
Deutsche Bank	DBK GY	EUR	15.9	14.5	-8.6%	17.8	12.9	59.0	31.2	0.8%	2.3%	3.5%	14.0	9.7	7.9	0.5	0.6	2.2	3.7	4.9	3.2	13.4
UniCredit	UCG IM	EUR	16.9	19.9	17.7%	18.4	9.7	50.9	37.1	1.7%	2.2%	3.3%	14.3	11.1	8.6	0.7	0.7	8.1	6.1	7.5	4.2	8.2
Mediobanka	MB IM	EUR	9.7	10.1	4.6%	10.0	6.3	58.0	7.8	4.2%	4.3%	4.5%	11.6	10.9	10.2	0.9	1.0	8.4	8.4	7.9	12.2	13.3
Intesa Sanpaolo	ISP IM	EUR	2.8	3.1	11.4%	3.0	2.0	49.1	48.7	7.1%	6.8%	7.1%	13.7	12.1	10.8	0.9	1.0	10.4	7.3	8.7	5.8	12.7
Emilia Romagna	BPE IM	EUR	4.6	5.3	14.5%	5.8	3.8	62.0	2.2	1.2%	2.0%	3.6%	15.8	9.1	7.0	0.4	0.5	2.2	3.1	6.9	6.8	13.8
UBI Banca	UBI IM	EUR	4.0	4.3	7.3%	4.6	1.9	56.4	4.7	2.5%	3.4%	4.7%	19.9	12.6	7.9	0.5	0.6	4.4	4.1	5.8	6.6	11.5
ING Groep	INGA NA	EUR	15.2	16.9	11.6%	16.1	12.4	38.6	61.4	4.6%	4.8%	5.0%	12.4	11.9	11.1	1.2	1.2	10.3	10.3	10.5	5.7	14.2
ABN Amro	ABN NA	EUR	24.9	27.4	9.9%	26.9	19.9	45.3	22.5	5.5%	5.5%	6.0%	10.3	10.6	10.2	1.1	N. A.	13.2	11.0	10.8	4.7	17.1
DNB	DNB NO	NOK	151.7	162.6	7.2%	164.3	125.2	40.5	27.1	4.5%	5.2%	5.8%	12.9	11.7	10.7	1.3	1.3	9.9	10.5	11.1	7.0	16.0
BBVA	BBVA SQ	EUR	7.2	7.5	4.2%	7.9	5.7	49.2	51.0	3.7%	3.8%	4.2%	12.0	11.1	10.3	1.0	1.2	8.9	8.9	9.2	5.2	12.1
Santander	SAN SQ	EUR	5.6	6.0	6.6%	6.2	4.1	53.9	85.4	3.6%	3.8%	4.2%	12.6	11.4	10.2	0.9	1.3	7.3	8.1	8.8	4.7	12.5
Bankia	BKIA SQ	EUR	4.0	4.1	2.7%	4.7	3.3	58.0	12.3	3.2%	3.5%	4.2%	13.4	12.6	11.4	0.9	N. A.	6.6	6.7	7.5	6.6	14.7
Bankinter	BKT SQ	EUR	8.1	7.9	-2.3%	8.8	7.0	65.7	7.4	3.2%	3.6%	3.8%	15.7	14.5	13.0	1.7	1.8	11.4	12.0	12.5	5.8	11.8
Sabadell	SAB SQ	EUR	1.7	1.8	4.8%	2.0	1.2	54.9	10.6	3.4%	4.1%	4.9%	13.7	11.8	10.0	0.7	0.9	6.4	6.4	7.3	5.2	12.0
CaixaBank	CABK SQ	EUR	4.0	4.3	7.9%	4.5	2.7	52.8	26.4	3.6%	4.5%	5.0%	15.3	12.5	11.2	1.0	1.2	7.7	8.7	9.3	5.8	N. A.
SEB	SEBA SS	SEK	99.4	111.7	12.4%	109.0	90.1	40.8	23.5	5.8%	6.0%	6.4%	13.0	12.5	11.7	1.5	1.6	12.2	12.1	12.4	5.0	18.8
Handelsbanken	SHBA SS	SEK	114.4	119.4	4.4%	136.3	111.7	40.1	24.5	5.4%	5.3%	5.5%	14.7	14.2	13.5	1.6	1.7	11.7	11.6	11.8	4.8	25.1
Swedbank	SWEDA SS	SEK	199.9	222.7	11.4%	234.0	193.2	43.2	25.0	6.4%	6.4%	6.7%	12.7	12.2	11.7	1.7	2.0	14.5	14.0	14.1	5.4	25.0
Nordea	NDA SS	SEK	98.1	111.0	13.1%	115.7	95.1	38.6	43.3	0.7%	0.7%	0.7%	120.6	111.0	104.9	1.2	1.4	9.8	10.6	11.0	4.7	18.4
Julious Baer	BAER VX	CHF	57.8	61.7	6.8%	61.2	43.1	45.7	10.8	2.4%	2.9%	3.2%	15.4	13.7	12.4	2.4	5.1	14.1	14.8	14.7	2.7	16.4
Credit Suisse	CSGN VX	CHF	16.7	17.7	6.3%	17.1	12.3	67.5	33.4	2.1%	3.1%	4.1%	19.4	12.4	9.5	1.0	1.1	3.9	6.8	8.9	4.5	13.6
UBS	UBSG VX	CHF	17.0	18.7	10.3%	17.6	14.6	54.0	56.9	3.8%	4.3%	4.9%	12.4	11.6	10.4	1.2	1.3	8.2	9.5	10.2	5.1	16.8
Median					**7.2%**			**49.7**		**3.5%**	**3.8%**	**4.5%**	**12.8**	**11.8**	**10.5**	**1.0**	**1.2**	**8.4**	**8.5**	**9.0**	**5.2**	**13.6**

Source: Bloomberg

APPENDIX

Table 3. Calendar

Date	Region	Section	Event	Period
1-Dec	EU	Macro	Markit Eurozone Manufacturing PMI	Nov
1-Dec	US	Macro	Markit US Manufacturing PMI	Nov
1-Dec	US	Macro	ISM Manufacturing	Nov
1-Dec	US	Macro	Construction Spending MoM	Oct
4-Dec	EU	Macro	PPI	Oct
4-Dec	US	Macro	Factory Orders and Durable Goods	Oct
5-Dec	EU	Macro	Markit Eurozone Services and Composite PMI	Nov
5-Dec	EU	Macro	Retail Sales	Oct
5-Dec	**EU**	**Macro**	**GDP**	**3Q**
5-Dec	US	Macro	Trade Balance	Oct
5-Dec	US	Macro	Markit US Services and Composite PMI	Nov
6-Dec	US	Macro	ADP Employment Change	Nov
8-Dec	**US**	**Macro**	**Nonfarm Payrolls and Employment report**	**Nov**
8-Dec	US	Macro	U. of Mich. Sentiment	Dec
12-Dec	EU	Macro	ZEW Survey Expectations	Dec
12-Dec	US	Macro	PPI	Nov
13-Dec	EU	Macro	Industrial Production	Oct
13-Dec	EU	Macro	Employment	3Q
13-Dec	US	Macro	CPI	Nov
13-Dec	**US**	**Macro**	**FOMC Rate Decision**	**Dec 13**
14-Dec	EU	Macro	Eurozone Manufacturing and Composite PMI	Dec
14-Dec	**EU**	**Macro**	**ECB Main Refinancing Rate**	**Dec 14**
14-Dec	US	Macro	Retail Sales	Nov
14-Dec	US	Macro	Markit US Manufacturing PMI and Composite PMI	Dec
15-Dec	EU	Macro	Trade Balance	Oct
15-Dec	US	Macro	Empire Manufacturing	Dec
15-Dec	US	Macro	Industrial Production and Capacity Utilization	Nov
18-Dec	EU	Macro	CPI	Nov
18-Dec	US	Macro	NAHB Housing Market Index	Dec
19-Dec	US	Macro	Housing Starts and Building Permits	Nov
20-Dec	US	Macro	Existing Home Sales	Nov
21-Dec	EU	Macro	Consumer Confidence	Dec
21-Dec	US	Macro	FHFA House Price Index MoM	Oct
21-Dec	US	Macro	Leading Index	Nov
22-Dec	US	Macro	Personal Income and Spending	Nov
22-Dec	US	Macro	New Home Sales	Nov
22-Dec	US	Macro	U. of Mich. Sentiment	Dec
26-Dec	US	Macro	S&P CoreLogic CS 20-City	Oct
26-Dec	US	Macro	Richmond Fed Manufact. Index	Dec
26-Dec	US	Macro	Dallas Fed Manf. Activity	Dec
27-Dec	US	Macro	Conf. Board Consumer Confidence	Dec
27-Dec	US	Macro	Pending Home Sales MoM	Nov
28-Dec	US	Macro	Wholesale Inventories MoM	Nov
28-Dec	US	Macro	Chicago Purchasing Manager	Dec

Source: Bloomberg

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