

Modrá Pyramida

May 27, 2013

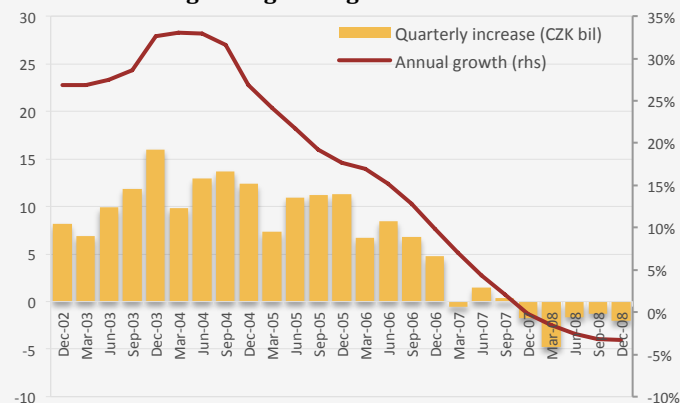
Quarterly Analysis of the Building Savings Banks

- The business remains under pressure in spite of its impressive profitability. ROE fell to 15.2% in 2012 and net profit dropped 6% yoy in 4Q
- Lending continues to fall and is losing to mortgages. In 4Q12, the annual decline deepened to 3.3% yoy
- 4Q12 confirmed a recovery in terms of the number of new contracts sold, while deposits grew by a seasonally strong 3.2% qoq
- ČMSS remains the leader, but Raiffeisen grabs most of the growth

Loan decline deepens in 4Q12...

Loans granted by building savings banks dropped a further 0.7% qoq in 4Q and deepened their annual decline to 3.3% yoy in 2012. Building savings continued to lose compared to traditional mortgage lending, which grew 2% qoq in 4Q and 6.3% yoy in 2012:

Chart 1: Building Savings loan growth



Source: ČNB, Company data, Helgi Analytics

Housing loans reached 21% of GDP at the end of 2012 and represented more than a third of the bank loans in the system. While the penetration of mortgage lending continues to increase (over 14% of Czech households has a mortgage loan now), the business model of building savings remains under pressure.

...as the market is already saturated...

With 4.3 mil existing contracts on the market, virtually every Czech household is already exposed to the building savings. Lower government subsidies and possible restrictions on using the deposits further reduce the attractiveness of building savings. The number of contracts is down 31.5% from its peak in 2003 and dropped a further 5% yoy and 0.3% qoq in 4Q.

...and clients switch to mortgage loans

While positive for mortgage lending, declining interest rates make lending by building savings banks less competitive. This, together with a lower yield from debt securities (accounting for 24% of assets) and a rigid funding structure (building savings banks pay a third more than the market on their borrowing) will probably result in increased margin pressure in 2013.

4Q's silver lining

Despite the negative momentum, building savings banks remain well profitable and cost-efficient. In 2012, the business generated ROE of over 15% and contributed around 7% to the bottom line of the banking sector. The main good news in 4Q comes from the confirmation of the positive momentum in terms of the number of new contracts sold. They increased by 5.5% in 2012.

ČMSS remains the leader, Raiffeisen grows the fastest

In spite of its seasonal weakness, ČMSS remains the undisputed leader, with over 40% of the market in 2012. On the other hand, the Raiffeisen savings bank was the only one whose loan book grew in 2012 and it grabbed most of the new deposits in 4Q.



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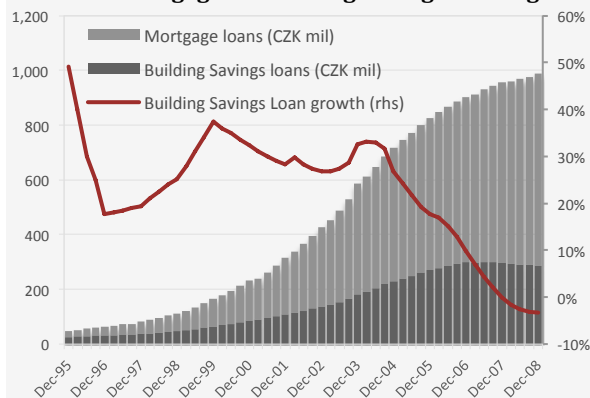
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Loan Growth & Market Share

Loan decline deepens in 4Q

Building savings banks' loan books dropped a further 0.7% qoq in 4Q and deepened their annual decline to 3.3% in 2012. Although mortgage lending growth continues to slow down as well (to as low as 6.3% yoy in 4Q), it is increasingly clear who the winner in the housing financing battle is:

Chart 2: Mortgage vs. Building Savings Lending

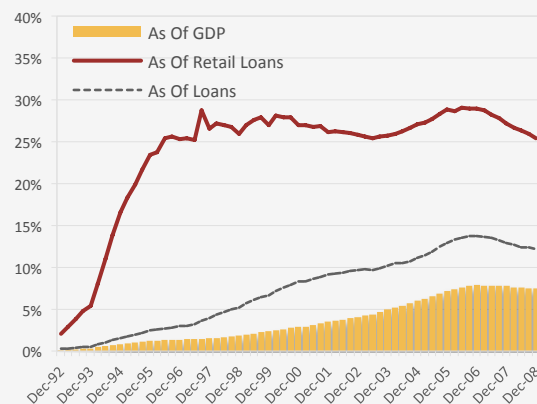


Source: ČNB, Ministry of Finance, Helgi Analytics

At the end of 2012, loans provided by the building savings banks represented 12.2% of total loans in the Czech banking system, down from the peak of 13.7% in 2010. Within the retail segment, building savings loans account for around a quarter of total loans now.

Apart from the gradual cuts in the state subsidy, which have been reducing the attractiveness of the building savings business, the relatively low size of building savings loans and more attractive pricing of mortgage lending seem to play increasingly against the building savings business, as shown in Chart 2 above.

Chart 3: Building Savings Loans



Source: ČNB, Ministry of Finance, Helgi Analytics

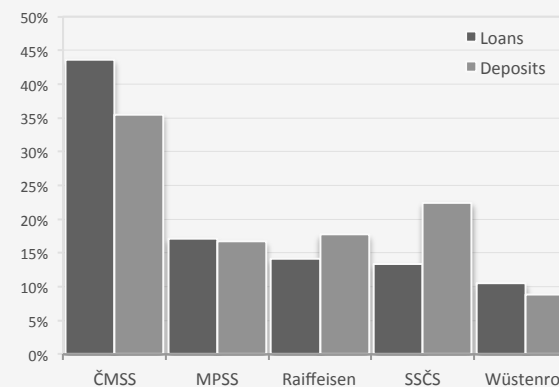
Structure of lending

The structure of the loan book has not changed much in recent years. The so-called “překlenovací úvěry”, which is an alternative to a traditional mortgage loan, represented over 80% of the total loans provided by the building savings banks. This is a similar share when compared to the situation five years ago (78% in 2007). Most of the new loans (more than 40%) are provided for reconstruction and modernisation of the existing housing stock, so building savings lending serves increasingly as a housing loan (a smaller and a more expensive one) that is complementary to traditional mortgage lending.

ČMSS maintains a big lead...

ČMSS remains the dominant player on the market, with a 43.6% share as of the end of 2012. The second largest player – Komerční Banka's Modrá Pyramida – is hardly a half of ČMSS's size, with a 17.1% of the market.

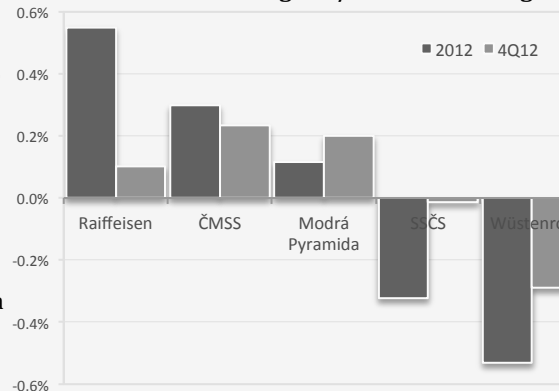
Chart 4: Market share of building savings, 2012



...but Raiffeisen is growing the fastest

Although ČMSS gained most of the market share in 4Q, the Raiffeisen building savings bank is the informal winner of the year 2012. Not only did it increase its market position most, but it was the only savings bank which was able to expand its loan book that year:

Chart 5: Market share gains/losses in lending



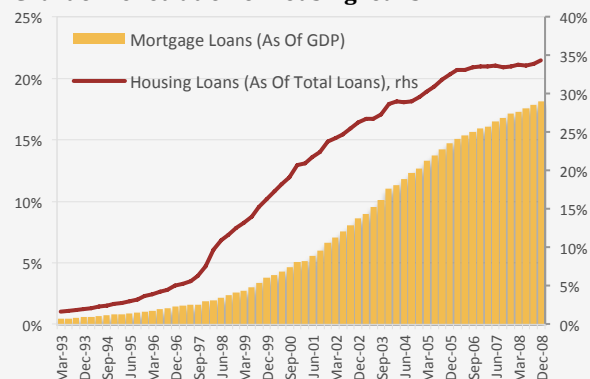
Source: Association of Building Savings, Banks, Helgi Analytics

Penetration & House Affordability

Housing loans represent 21% of GDP

Residential mortgage loans increased 6.3% yoy to CZK 700 bil in 4Q12 and represented 18.1% of GDP. Together with building savings loans, the total exposure of residential housing lending represented 21% of GDP and more than a third of total bank loans:

Chart 6: Penetration of housing loans



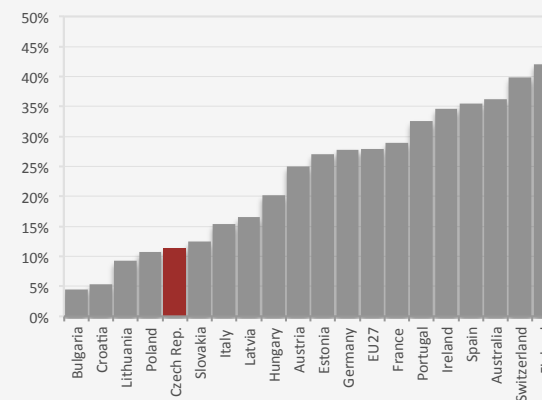
Source: ČNB, ČSÚ, Helgi Analytics

Some 14% of households have a mortgage loan..

The penetration of housing loans has continued to grow for over 15 years now. We estimate that approximately 14% of households in the Czech Republic had a mortgage loan at the end of 2012. In addition, every fifth Czech household had a loan from a building society at the year's end.

This is still relatively little when compared to the West, where around a third of families live with a mortgage loan. Czechs own most of the dwellings they live in (80%) and there is no shortage of housing stock, so mortgage lending growth is therefore fuelled by the desire to improve living standards rather than fulfilling basic needs.

Chart 7: Households with mortgage loans, 2010



Source: ČNB, ČSÚ, Eurostat, MMR, Helgi Analytics

Czechs remain fairly conservative worldwide – nearly all mortgage loans are CZK-denominated and the average loan-to-value ratio is only around 65%.

Housing affordability has been improving

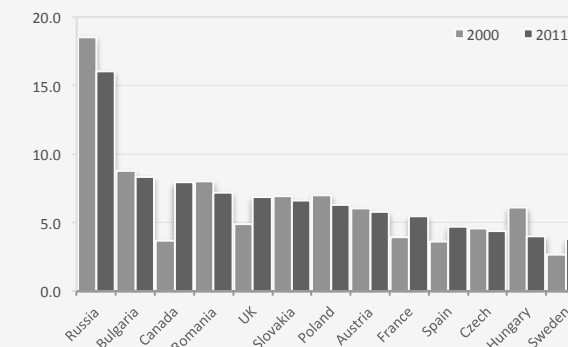
Czech real estate prices have tripled over the last decade in USD terms. The average dwelling (a 64-sqm flat) costs around USD 70,000 (or USD 1,047 per sqm) and one would pay roughly twice as much in Prague, the Czech capital city.

The affordability of housing has been improving since 2008, when real estate prices started falling. To buy an average-sized flat now would take an average earner over four annual gross salaries. This puts the Czech Republic among the cheapest places in Europe in terms of residential housing, alongside Hungary or Sweden, for example.

Big differences remain within the country, however. While a citizen of Prague has to put aside about eight annual salaries to buy an average flat, it takes slightly

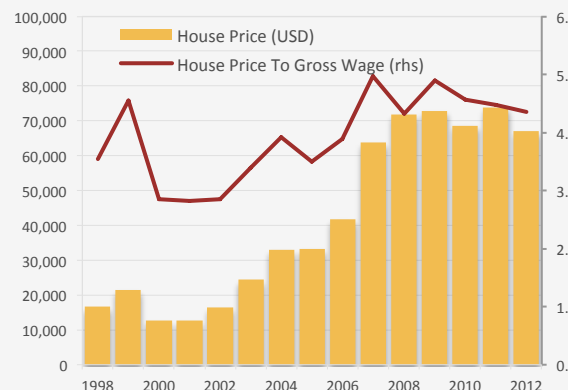
more than two years to save for a flat in Ústí nad Labem or in Ostrava.

Chart 8: House Affordability, International (years)



Source: ECB, ČNB, Eurostat, Statistical Offices, Helgi Analytics
When looking back, housing affordability in the Czech Republic has improved to the level last seen in 1999:

Chart 9: House Affordability, Czech Republic (years)



Source: ČNB, ČSÚ, Helgi Analytics

Loan Asset Quality

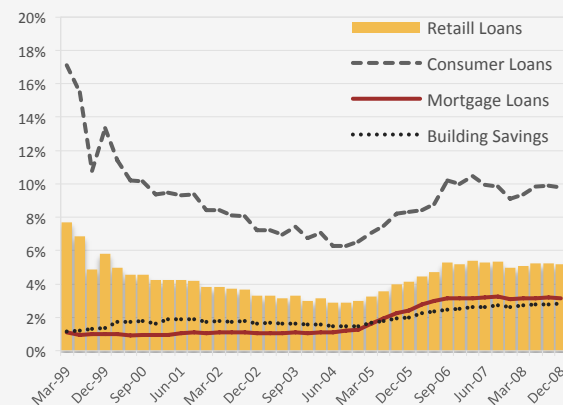
NPLs account for only 2.8% of total

Despite all the media fuss about the economic and financial crisis, the Czech economy remains fairly solid, the banking system strongly capitalised, well funded and profitable, real estate relatively cheap and the unemployment problem manageable.

The asset quality of housing loans therefore remains good. The volume of problem loans at savings banks increased by CZK 363 mil in 2012 (or CZK 52 mil in 4Q) to CZK 8.12 bil, and the proportion of problem loans rose marginally from 2.60% to 2.82% during the year.

This is lower than in the case of mortgage lending (with 3.1-3.2% during the year) and the lowest among all loan segments:

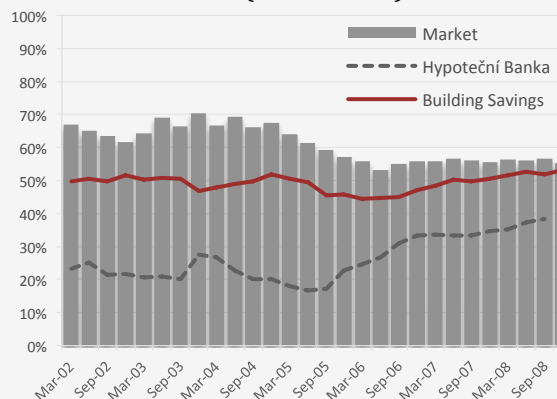
Chart 10: Non-performing loans (as % of total loans)



Source: ČNB, Banks, Helgi Analytics

The provision coverage remains solid at over 53% of non-performing loans, which is very close to the whole banking sector's average (at 55% at the year's end). This is also well above the 35-40% seen with pure mortgage lenders (Hypoteční and Wüstenrot).

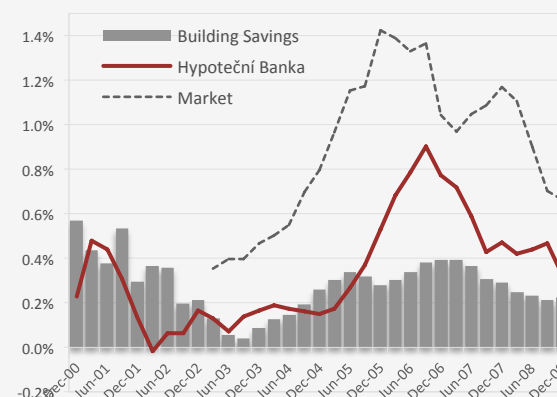
Chart 11: Provisions (as % of NPLs)



Source: ČNB, Banks, Helgi Analytics

More importantly for the bottom line, the cost of risk has fallen further, to 23 bp in 2012. This is compared to 29 bp in 2011 and 39 bp in 2010 and is also well below the overall market (with 66 bp of average loans in 2012):

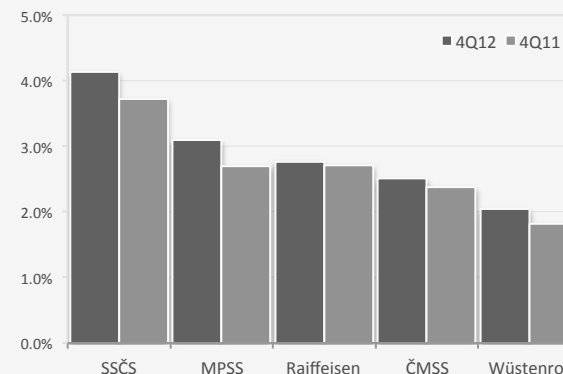
Chart 12: Cost of Risk



Wüstenrot – the asset quality champion

The proportion of non-performing loans ranges from 2.04% of total loans at Wüstenrot to 4.13% at Stavební Spořitelna České Spořitelny in 4Q12. Interestingly, the relatively high proportion of bad loans at Česká Spořitelna is not a result of asset quality deterioration (Spořitelna's NPLs increased the least among all the building societies), but of a 13% fall in total loans (the denominator of the formula) since 2009:

Chart 13: Provisions (as % of NPLs)



Source: ČNB, Banks, Helgi Analytics

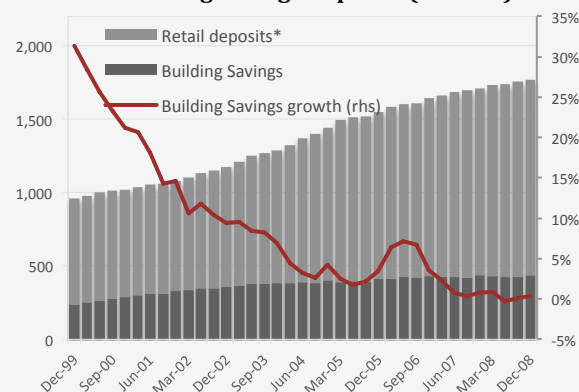
Thanks partly to its superior asset quality, Wüstenrot is also the building saving bank with the highest provision coverage of bad loans. At the end of 2012, nearly 68% of Wüstenrot's NPLs was covered by provisions, as opposed to ČMSS, where provisions accounted for only 42.5% of NPLs.

Deposit Growth & Market Share

Deposits grow 3.2% qoq in 4Q

Building Savings' deposits increased 3.2% qoq in the seasonally strongest quarter of the year to nearly CZK 435 bil. Although the overall growth continues to slow down, or has disappeared in the last year, building savings still represent an impressive 13.9% of total deposits in the Czech banking system and a quarter of total retail deposits:

Chart 14: Building Savings Deposits (CZK mil)



Source: ČNB, Helgi Analytics, *Excl. Building Savings

Unlike on the lending side, declining interest rates are good news for building savings deposits. Thanks to the “guaranteed” interest rate, the average cost of funding of building savings banks amounted to 2.16% at the end of 2012. This is a third higher than the average Czech bank pays and twice as much as at the three largest banks in the country.

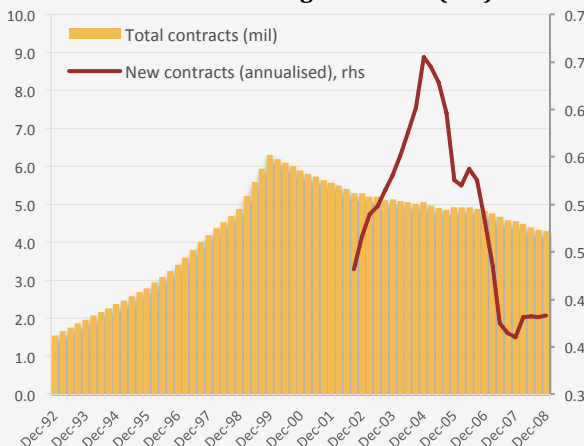
Together with the annual government subsidy of CZK 2,000, building savings probably offer the best term deposit product on the market, yielding over 3.5% p.a., however limited in size.

Sales of new contracts rise 5.5% in 2012

The increasingly attractive yield could be the reason why depositors are coming back to building saving deposits. In 4Q, sales of new building savings contracts reached 134,433, up 5.5% yoy when the last four quarters are summed up.

Although the total number of accounts is nearly 32% off its peak in 2003, the fall has stabilised in recent quarters:

Chart 15: Number of savings contracts (mil)

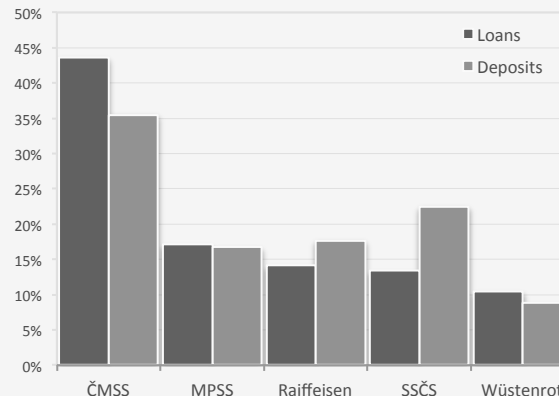


Source: ČNB, Company data, Helgi Analytics

ČMSS maintains the lead...

ČMSS maintains a comfortable lead within the five building savings banks; however, its 35.1% share is not as dominant as the 43.6% on the lending side. Still, Česká Spořitelna's savings subsidiary, the second largest deposit player with 22%, remains well behind.

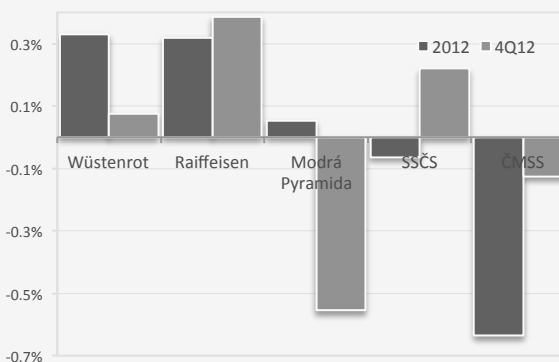
Chart 16: Market share of building saving societies



...but Raiffeisen gets most of the growth in 4Q

Similarly to the lending side, the Raiffeisen savings bank was the most aggressive one in terms of deposit collection in 4Q12, stealing mainly from Modrá Pyramida and ČMSS. In 4Q alone, the bank increased its market share by almost 0.4%:

Chart 17: Market share gains - deposits



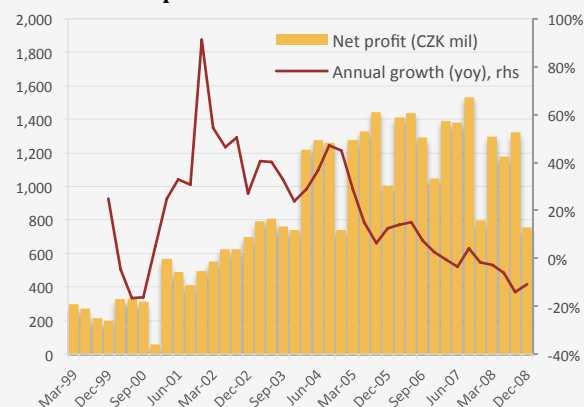
Source: ČNB, Banks, Helgi Analytics

Profitability

Profitability growth disappears...

The profitability of the building savings banks dropped a further 5.6% yoy to CZK 753 mil in 4Q and extended the annual fall to 10.8% for the full year 2012:

Chart 18: Net profit momentum



Source: ČNB, Company data, Helgi Analytics calculation

In spite of the negative momentum, the profitability of the building savings sector remains strong. Profits remain high in absolute terms, while ROE still exceeds 15%. Apart from the relatively solid macroeconomic picture, building societies benefit from:

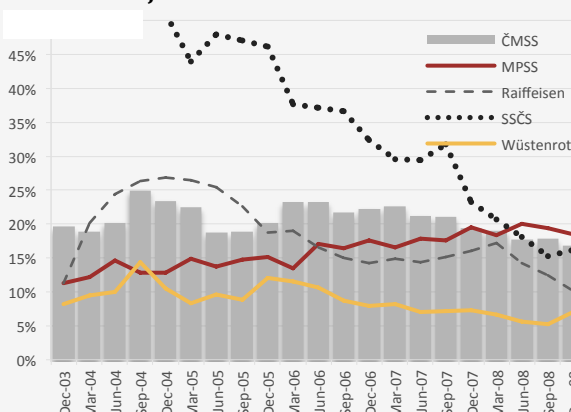
- ✓ **Regulatory environment** – which made the building savings business attractive through state subsidies and created high barriers to entry for competition
- ✓ **Economies of Scale** – the fast growth in the volume of deposits and loans in the last decade changed the economics of the business. Costs account for only 0.7% of assets and 35% of income, 30-50% lower than the average in the banking sector
- ✓ **Good asset quality** – with NPLs accounting for only

2.8% of total loans (compared to 6.2% in the system) and the cost of risk at only 23 bp (compared to 66 bp in the sector), building savings banks are exposed to the best-quality class of retail loans.

- ✓ **Strong capitalisation and funding** – with capital adequacy at 16.4% and loans to deposits at only 64%, building savings banks enjoy a remarkable position within the current banking world

When profitability is adjusted for a different level of capital, i.e. when the ROE of each building savings bank is re-calculated to the sector's average capital adequacy of 16.4%, Komerční Banka's Modrá Pyramida emerges as the most stable and profitable building savings bank:

Chart 19: Adjusted ROE



Source: ČNB, Company data, Helgi Analytics calculation

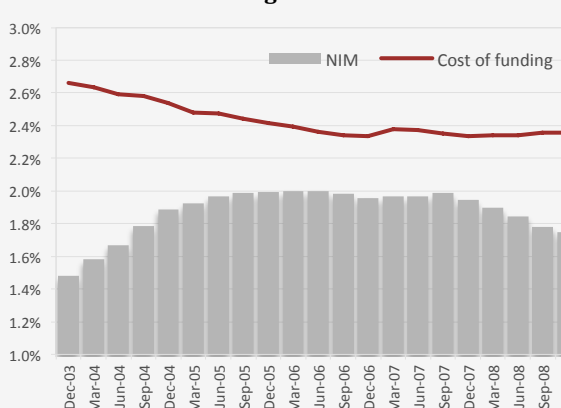
...while many challenges lie ahead

However good the current situation and profitability might appear, the risks are clearly on the downside. The key challenges the building savings business will have to cope with in the coming quarters will be:

- 1) **Decline in interest rates** – which makes building savings lending less competitive against mortgage loans, reduces yield from debt securities (24% of assets) and further hurts banks' interest margin thanks to the rigid funding structure.
- 2) **Regulatory changes** – opening up the building savings business to other banks and restricting the use of the clients' deposits will increase competition and will further reduce the attractiveness of the business.
- 3) **Slowdown in growth** – from the competitive mortgage loans, increased competition pressure and slowdown in the economy.

Having said that, there is a hidden value in the building savings business – a wide network of sales agents. However difficult to quantify, the addition of new products such as mortgage and consumer loans or insurance to the portfolio of building savings' products might bring synergies to banks' strategic partners.

Chart 20: Interest Margin



Source: ČNB, Company data, Helgi Analytics calculation

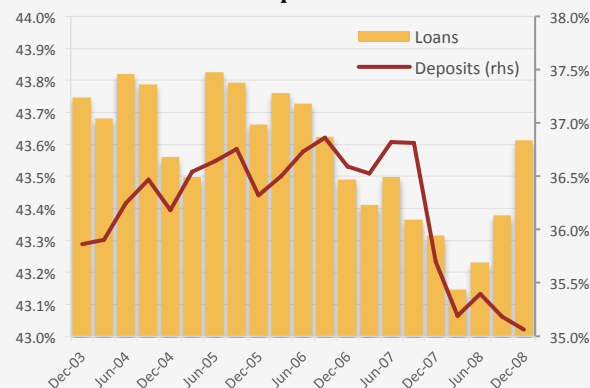
Game Of Thrones

Here, we provide a brief overview of the five building savings players and their performance in 2012 and 4Q. Ultimately, we try to point out the biggest gains and losses on the building savings chessboard in the last 12 months. We describe each bank's performance in more detail at the end of the report (starting on page 14).

ČMSS – the undisputed King

ČMSS, is the dominant leader of the building savings market, with a 43.6% in building loans and 35.1% in building savings as of the end of 2012. While the bank gained market share in lending in both 2012 (it added 30 bp) and 4Q12 (23 bp), the bank has been losing market share on the savings deposit market since the end of 2011:

Chart 21: ČMSS's market position



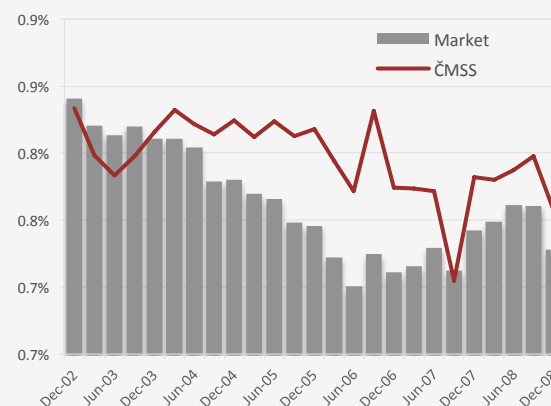
Source: ČMSS, ČNB, Helgi Analytics

Not that it matters, as ČMSS's market position is truly unique.

What matters, however, is the bank's profitability and efficiency. Given its superior market position, one would expect the bank's efficiency and profitability to be significantly above the market, as suggested by the example of Hypoteční Banka in the mortgage lending business. First, it is not the case, however impressive the return on equity of 18% is. Second, the trend is negative, which is more visible when the bank's numbers are compared to those of Modrá Pyramida (see chart 19 on page 6).

With revenue generation and the cost of risk better than the market average, it is clearly the cost side which might be hiding potential for improvement. How much this could be because of the bank's business model (ČSOB owns "only" 55% of the bank) and how much is due to low efficiency is something we try to quantify on page 14:

Chart 22: ČMSS's costs to assets



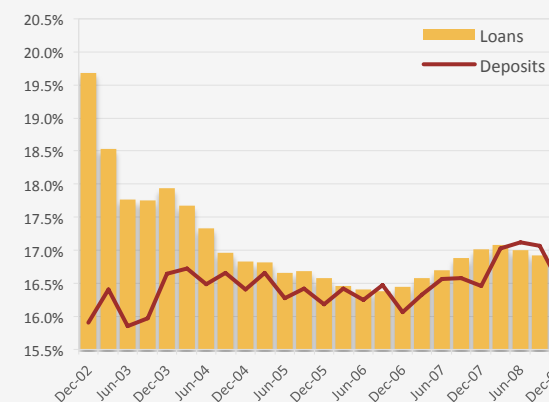
Source: ČMSS, Banks, Helgi Analytics

Modrá Pyramida – the good pupil of Komerční

Modrá Pyramida, fully owned by Komerční Banka, is the second largest building savings bank, with a 17.1% share of lending and a 16.5% share of building savings deposits.

The bank gained approximately 20 bp market share in loans in 4Q12, twice as much as for the full year 2012, but on the other hand, it lost the most out of all five building savings banks on the deposit side – 55 bp in 4Q12, by our calculation.

Chart 23: Modrá Pyramida's market position



Source: Modrá Pyramida, ČNB, Helgi Analytics

Following the full takeover by Komerční Banka in 2006, Modrá Pyramida has been improving its profitability and is now the most profitable building savings bank (when ROE is adjusted for overcapitalisation), although this is partly due to its low tax bill. The improvement is visible in the development of the market share, as the bank has been gaining market share in both loans and sales since 2011.

Game Of Thrones

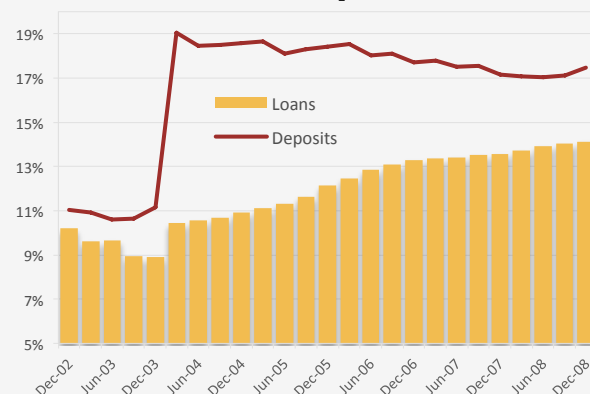
Raiffeisen Stavební Spořitelna

Raiffeisen is the third largest building savings bank and is partly owned by the Czech subsidiary of Raiffeisenbank (10%). Following the acquisition of Hypo Stavební Spořitelna in 2008, the building savings bank now owns 14.1% in building savings loans and 17.5% in deposits.

In 2012, Raiffeisen was the only building savings bank able to expand its loan book (albeit by only 0.6% yoy), so it increased its market share by 55 bp (and 10 bp in 4Q alone).

On the deposit side, Raiffeisen was also among the most aggressive banks, gaining a further 38 bp in 4Q (and 32 bp for the full year 2012):

Chart 24: Raiffeisen's market position



Source: Company data, ČNB, Helgi Analytics

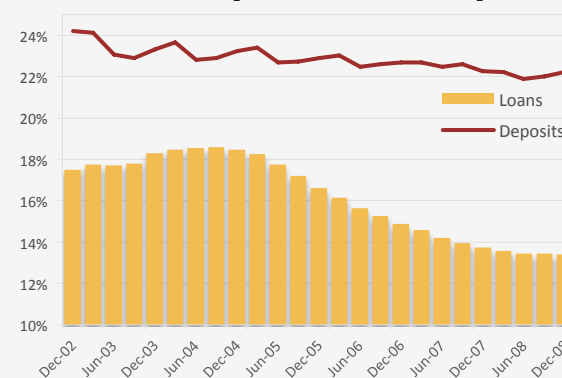
Stavební Spořitelna České Spořitelny

Once the second largest building savings bank on the market (with a share of nearly 19% of lending in 2008), the subsidiary of Česká Spořitelna has been losing its position in housing lending as part of the overall strategy of Česká Spořitelna to retreat from the area of housing finance as the financial crisis came.

The difference compared to the past (the bank holds 13.4% of the lending market now) could also be demonstrated by the bank's position on the building savings deposit market, where the bank still maintains an impressive 22% share.

Within the year 2012, the bank continued losing its market share in terms of both loans and deposits, though 4Q suggested a stabilisation of the overall bank's position (with a gain of 22 bp in deposits and a flattish change in loans):

Chart 25: Stavební Spořitelna ČS – market position



Source: Company data, ČNB, Helgi Analytics

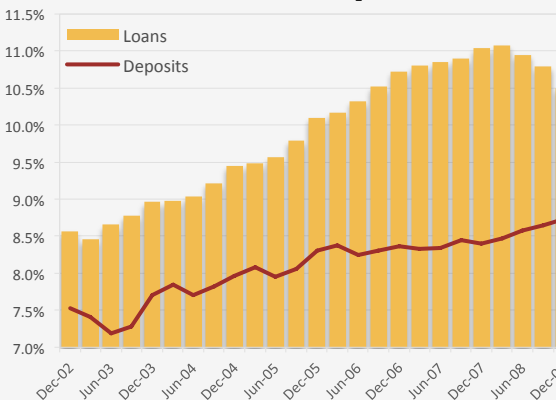
Wüstenrot – small but growing

Similarly to Wüstenrot Hypoteční banka in mortgage lending, Wüstenrot Stavební Spořitelna is a relatively little bank, with a 10.5% share of lending and 8.7% of building savings deposits as of the end of 2012.

Partly because of its small size (and limited economies of scale and synergies with a would-be commercial bank on the Czech market) and its conservative approach (the bank has the best loan quality and provision coverage), the bank is traditionally the least profitable building savings bank on the market. In 2012, the bank achieved ROE of “only” 9.7%, compared to the 15.2% of the 5-building savings banks average.

But the bank has been consistently building up its market position and has gained 1-2% of the market in the last 6 years. In 2012, however, Wüstenrot was the biggest loser on the loan market (with market share falling by more than 50 bp), while the bank gained over 30 bp in deposits:

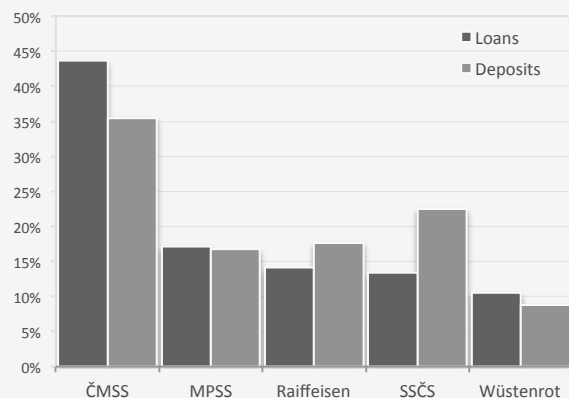
Chart 26: Wüstenrot's market position



Source: Company data, ČNB, Helgi Analytics

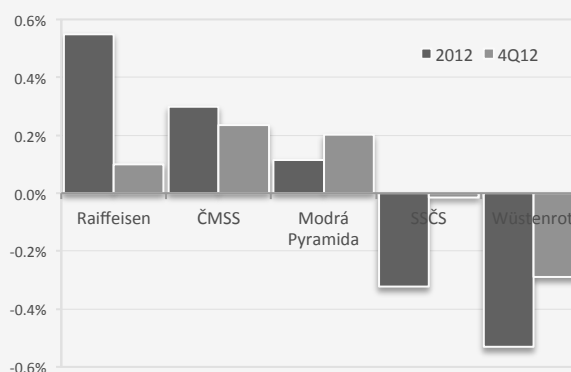
Building Savings Banks in Pictures

Chart 27: Market share (Loans & Deposits)



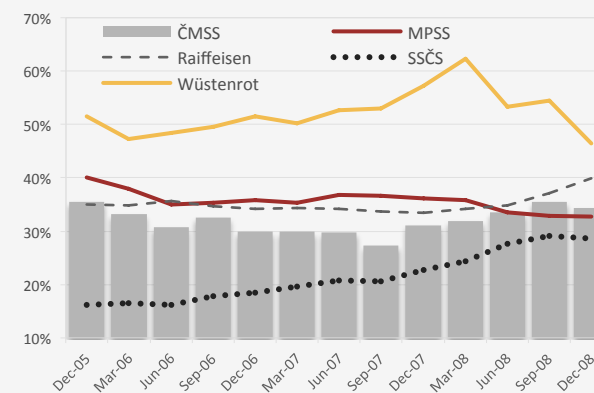
Source: Company data, Association of Building Savings Banks, Helgi Analytics

Chart 28: Market share gains/losses - loans



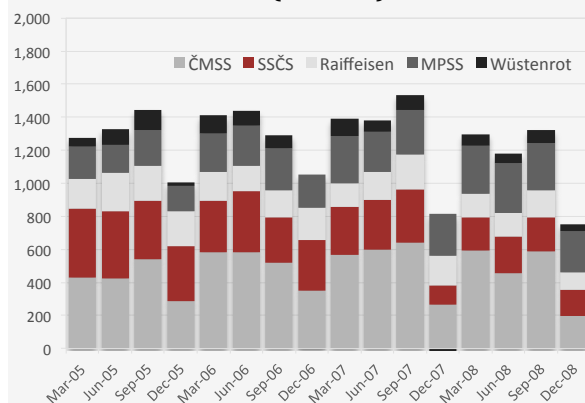
Source: Company data, Association of Building Savings Banks, Helgi Analytics

Chart 29: Costs to income



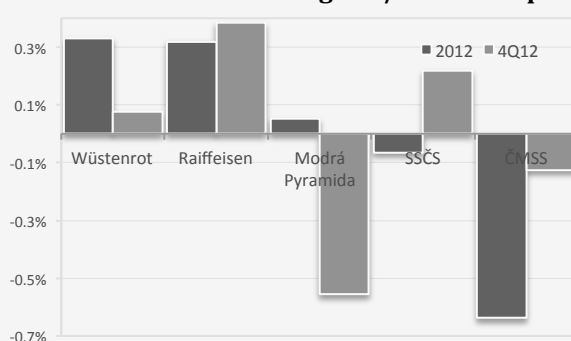
Source: Company data, Association of Building Savings Banks, Helgi Analytics

Chart 30: Net Profit (CZK mil)



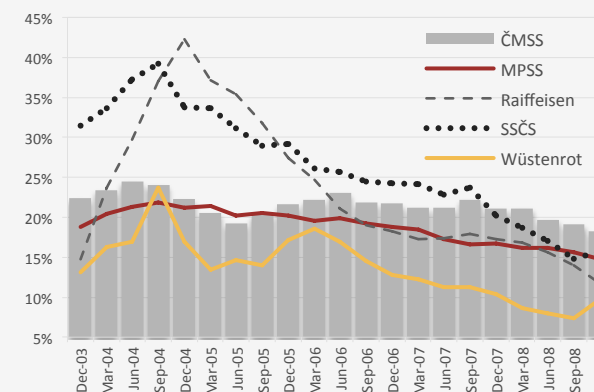
Source: Company data, Helgi Analytics

Chart 31: Market share gains/losses - deposits



Source: Company data, Ministry of Finance, Helgi Analytics

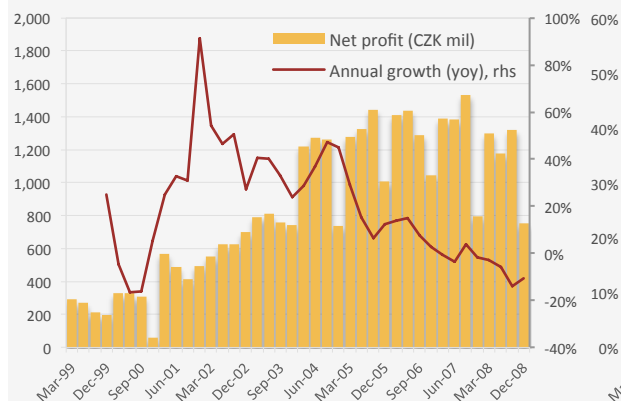
Chart 32: Return on equity



Source: Company data, Helgi Analytics

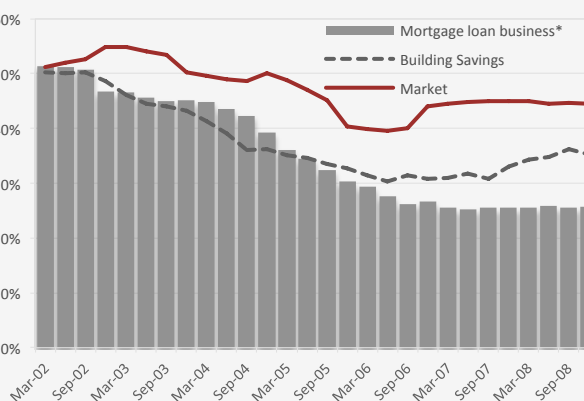
Building Savings Banks in Pictures

Chart 33: Net profit



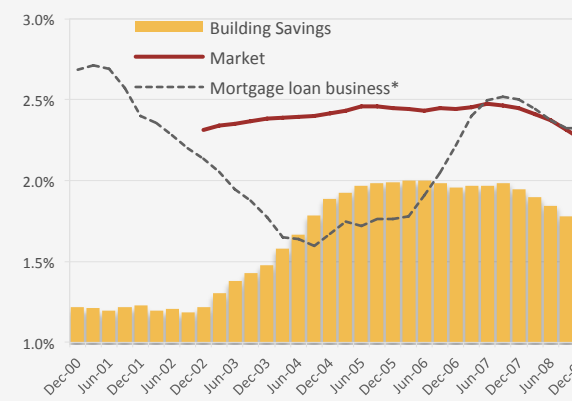
Source: Company data, Helgi Analytics

Chart 34: Costs to Income



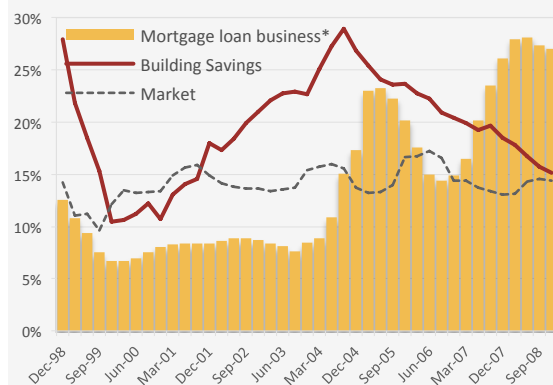
Source: Company data, Helgi Analytics

Chart 35: Net interest margin



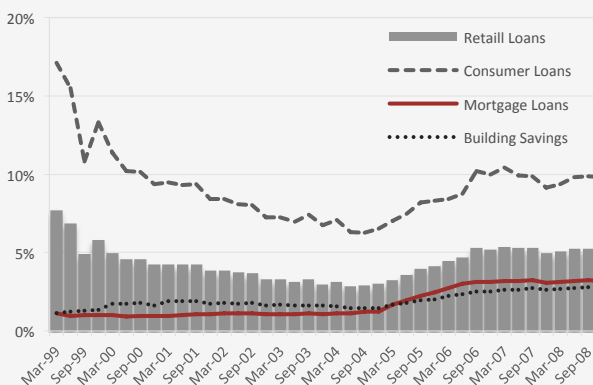
Source: Company data, Helgi Analytics

Chart 36: ROE



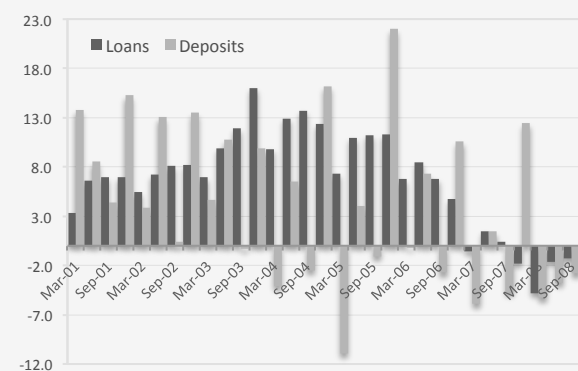
Source: Company data, Helgi Analytics

Chart 37: Asset quality (NPL Ratio)



Source: Company data, ČNB, Helgi Analytics

Chart 38: Quarterly growth(CZK bil)



Source: Company data, Helgi Analytics

Building Savings Societies – Key Financials

Table 1: Key characteristics of Czech building savings

	4Q10	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12
Housing Loans (As % Of GDP)	19.2%	19.2%	19.5%	19.7%	20.1%	20.2%	20.4%	20.7%	21.0%
Mortgage Loans (As % Of GDP)	15.9%	16.1%	16.5%	16.8%	17.2%	17.3%	17.6%	17.8%	18.1%
Building Society Loans (As % Of GDP)	7.8%	7.8%	7.8%	7.8%	7.7%	7.6%	7.6%	7.5%	7.5%
Asset Yield	4.21%	4.20%	4.19%	4.18%	4.15%	4.10%	4.06%	3.99%	3.90%
Cost Of Funding	2.38%	2.37%	2.35%	2.33%	2.34%	2.34%	2.36%	2.36%	2.30%
Net Interest Margin	1.96%	1.97%	1.97%	1.99%	1.94%	1.90%	1.85%	1.78%	1.75%
Costs To Income	30.8%	31.0%	31.8%	30.8%	33.1%	34.3%	34.8%	36.3%	35.2%
Costs To Assets	0.71%	0.72%	0.73%	0.71%	0.74%	0.75%	0.76%	0.76%	0.73%
NPLs (As Of Mortgage Loans)	3.1%	3.2%	3.2%	3.3%	3.1%	3.1%	3.2%	3.2%	3.2%
NPLs (As Of Building Savings Loans)	2.5%	2.6%	2.6%	2.7%	2.6%	2.7%	2.8%	2.8%	2.8%
Provision Coverage	47.0%	48.5%	50.3%	49.6%	50.6%	51.5%	52.6%	51.9%	53.1%
Cost Of Risk	0.39%	0.39%	0.37%	0.31%	0.29%	0.25%	0.23%	0.21%	0.23%
ROE	20.4%	19.9%	19.3%	19.7%	18.5%	17.8%	16.8%	15.7%	15.2%
ROA	1.11%	1.11%	1.09%	1.15%	1.09%	1.06%	1.02%	0.97%	0.96%
Mortgage Loan Contracts	501,545	515,678	535,691	552,741	572,633	589,723	608,785	625,680	646,228
Average Size Of Mortgage Loan (CZK mil)	1.21	1.19	1.18	1.16	1.15	1.13	1.11	1.10	1.08
Households With a Mortgage Loan	11.3%	11.6%	12.1%	12.4%	12.8%	13.2%	13.6%	13.9%	14.4%
Residential Dwellings With a Mortgage Loan	11.0%	11.3%	11.7%	12.0%	12.4%	12.8%	13.2%	13.6%	14.0%
Building Society Loan Contracts	993,357	985,221	981,359	973,450	956,659	939,557	927,360	913,424	894,358
Average Size Of Building Society Loan (CZK mil)	0.300	0.302	0.305	0.308	0.311	0.312	0.314	0.317	0.322
Households with a Building Society Loan	22.5%	22.2%	22.1%	21.9%	21.4%	21.0%	20.7%	20.3%	19.9%
Building Society Deposit Contracts	4,845,319	4,757,301	4,663,792	4,592,720	4,550,468	4,491,711	4,403,435	4,329,383	4,316,999
Average Size Of Building Society Deposit (CZK)	0.433	0.431	0.434	0.432	0.453	0.456	0.458	0.462	0.486
Households With Building Society Deposits	110%	107%	105%	103%	102%	100%	98%	96%	96%
Loans To Deposits (Of Building Societies)	69.3%	70.1%	70.2%	71.1%	68.7%	68.4%	68.6%	68.8%	66.2%

Source: ČNB, ČSÚ, MMR, Ministry of Finance, Association of Building Societies, Company data, Helgi Analytics

Do Economies of Scale & Market Power matter?

ČMSS dominates the building savings market, with a 43.6% share of loans and 35.1% of deposits. At the same time, building savings have risen to a decent size, representing 10% of the total sector assets. This is reminiscent of the situation of Hypoteční Banka, which is the largest player on the Czech mortgage lending market and probably the most profitable part of the Czech banking system now.

It might therefore be interesting to see:

- ✓ if the efficiency and profitability of ČMSS increase with rising volumes
- ✓ if the leading market position of ČMSS translates into superior profitability and efficiency

We therefore compare ČMSS's financials with the rest of the sector and put them into perspective with Hypoteční Banka's experience from the mortgage market.

Here are the main conclusions from the exercise:

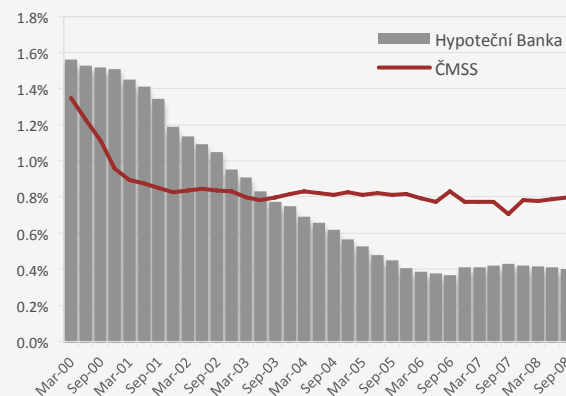
Size matters...

Both ČMSS and Hypoteční Banka show a remarkable improvement in their cost-efficiency as loans and assets rise to meaningful levels.

When looking at chart 39 on the right, you will see that the costs-to-assets ratio of ČMSS has dropped by half since the end of 2004, while the volume of loans has increased 4-5 times.

In the case of Hypoteční Banka, the ratio dropped to a third of around 0.4% as of September 2012, a remarkable improvement:

Chart 39: Costs to Assets



Source: Company data, Helgi Analytics

...but market leadership not necessarily

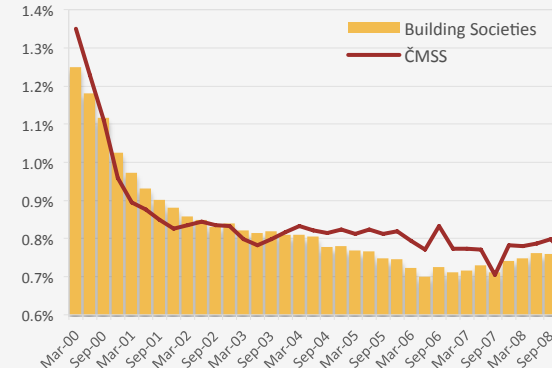
Hypoteční Banka is a success story to follow. With a market share of nearly 26% of the mortgage market and an ROE that we calculate as 25-30% in the last three years, the bank is one of the most profitable parts of the Czech banking system now.

ČSOB's superior profitability (as it has one of the largest exposures to mortgage lending) and the difference in efficiency and profitability between the market leader Hypoteční and Wüstenrot suggest the conclusion that market share matters in mortgage lending.

Surprisingly, this is not the case with ČMSS. Although the bank shows above-average profitability when measured by ROE, the difference is not significant enough to draw any strong conclusions. But, when adjusted for capital surplus, ČMSS is not the most profitable building savings bank on the market any more.

The cost side seems to be the main weakness of ČMSS when compared to others as costs account for 76% of average assets, compared to the market average of 73%:

Chart 40: Costs to Assets



Source: Company data, Helgi Analytics

ČMSS seems to be paying more than its competition (by a quarter on our estimates), so weak cost control could be a specific problem of the bank.

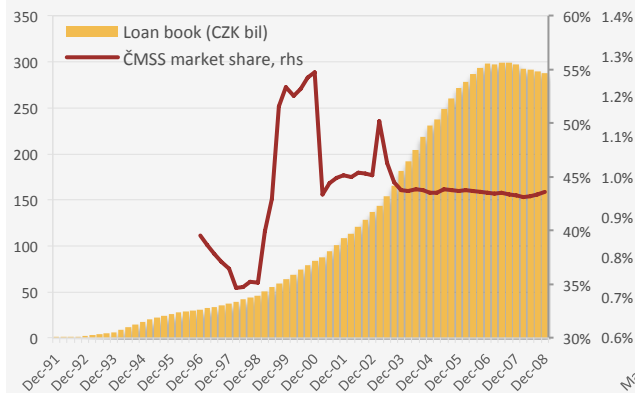
Watch for synergies and business model!

A more difficult question is the effect of a business model. While the building savings bank of Komerční Banka (Modrá Pyramida), for example, is managed as a part of the bigger financial group, which might offer numerous synergies, ČMSS seems to be following a more independent business model.

As the building savings business is to open up to newcomers and the sales network of current building societies will be drawn into offering traditional banking products, the question of the business model and synergies with a strategic partner will become the main feature to follow in the coming quarters.

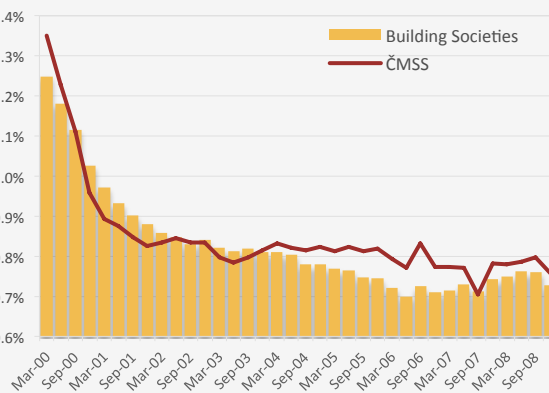
ČMSS & Hypoteční Banka – Monetisation of Leadership

Chart 41: Building Savings loans



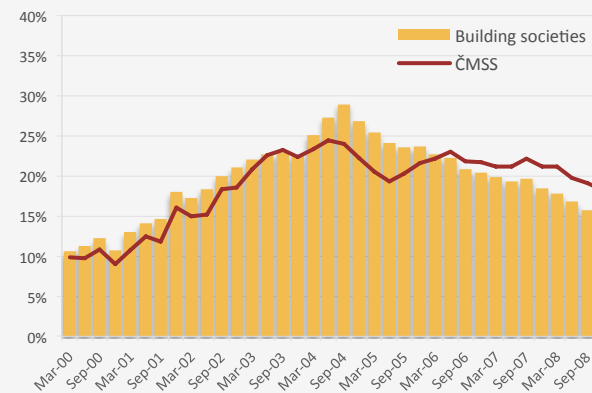
Source: Company data, Helgi Analytics

Chart 42: Costs to assets (Building Savings)



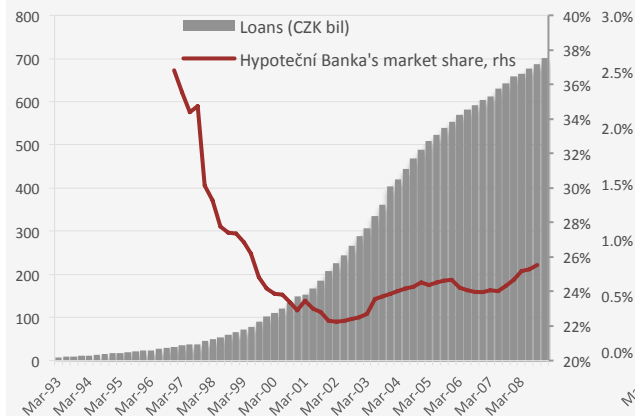
Source: Company data, Helgi Analytics

Chart 43: ROE (Building Savings)



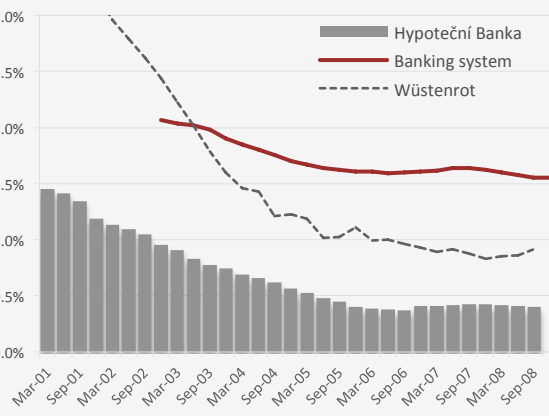
Source: Company data, Helgi Analytics

Chart 44: Mortgage loans



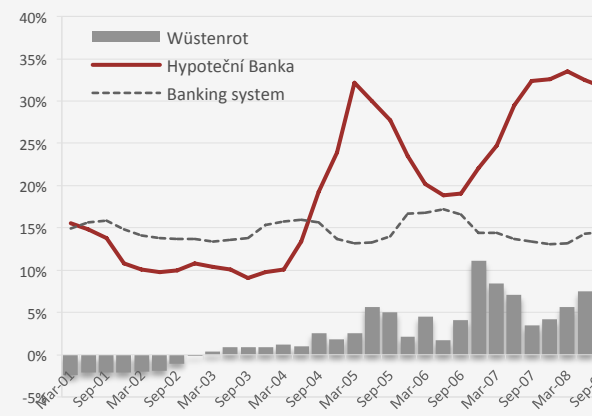
Source: Company data, Helgi Analytics

Chart 45: Costs to assets (Mortgage Lending)



Source: Company data, Helgi Analytics

Chart 46: ROE (Mortgage Lending)



Source: Company data, Helgi Analytics

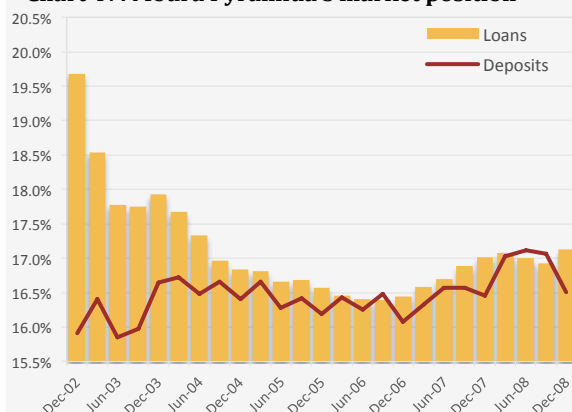
Modrá Pyramida

Market position

Modrá Pyramida, fully owned by Komerční Banka, is the second largest building savings bank, with a 17.1% share of lending and a 16.5% share of building savings deposits.

The bank gained a market share of approximately 20 bp in loans in 4Q12, twice as much as for the full year 2012, but on the other hand, it lost the most out of all five building savings banks on the deposit side – 55 bp in 4Q12, by our calculation (but gained 5 bp in the full year 2012):

Chart 47: Modrá Pyramida's market position



Source: Company data, Ministry of Finance, Helgi Analytics

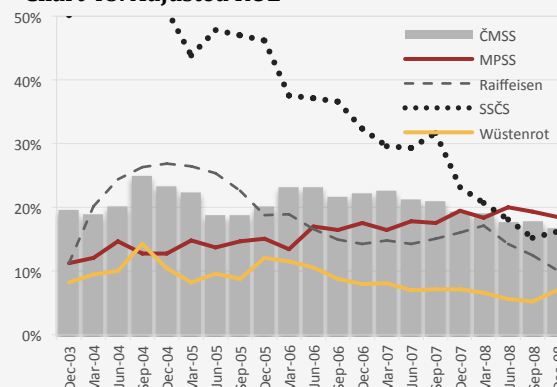
Despite gaining market share over the last two years, the bank's overall balance sheet momentum remains negative. Loans declined by a further 1.2% qoq in the last quarter and the full-year decline reached 4.3% yoy, while overall deposits dropped 1.7% in 4Q and were flat in 2012.

Profitability

Modrá Pyramida remains impressively profitable in spite of the market slowdown. In 2012, the bank achieved ROE of 14.2%, which is a remarkable achievement given the fact that the bank's capital adequacy has been exceeding 20%, the highest figure on the market.

When adjusted for surplus of capital (when ROE is adjusted to the building savings market average for each bank), Modrá Pyramida becomes the most profitable building savings bank on the market:

Chart 48: Adjusted ROE



Source: Company data, Helgi Analytics

Part of Modrá Pyramida's superior profitability, however, is helped by a low tax burden. Thanks to its structure of debt securities, the bank's effective tax rate is 8.5% over the last three years, half of the sector average.

Asset quality

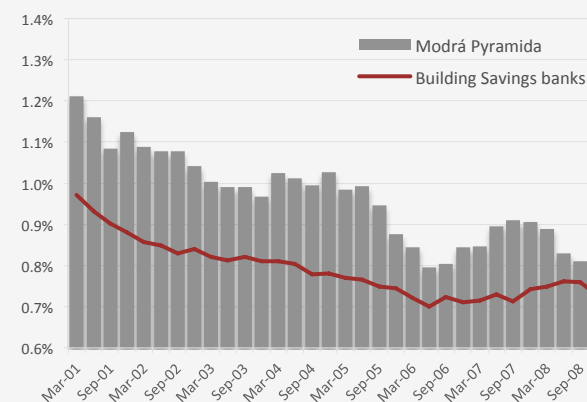
Non-performing loans rose CZK 45 mil, or 3.0%, in 4Q and reached 3.09% of total loans (up from 2.70% at the end of 2011). Provision coverage remains relatively solid

at nearly 62%, compared to the 53% of the market.

Cost-efficiency

Similarly to ČMSS, the market leader, Modrá Pyramida seems to be less cost-efficient than the other savings banks. Operating costs accounted for 0.80% of average assets at Modrá Pyramida in 2012, more than the 0.73% seen on the market. On the other hand, Modrá Pyramida's cost-to-income ratio is better than the market (again, similar to ČMSS).

Table 49: Costs to Assets



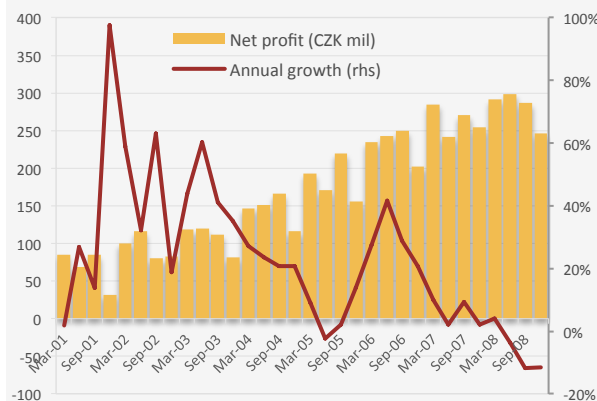
Source: Company data, Helgi Analytics

Being the two strongest lenders on the market (alongside ČMSS), it suggests that lending activity is relatively cost-demanding, but rewarded on the revenue side and in the bank's bottom line.

Closer cooperation with Komerční Banka following the takeover in 2006 seems to be bearing fruit, so a further tie-up of Pyramida's sales network with Komerční's products (and the fees generated from that) will be interesting to watch for in the coming quarters.

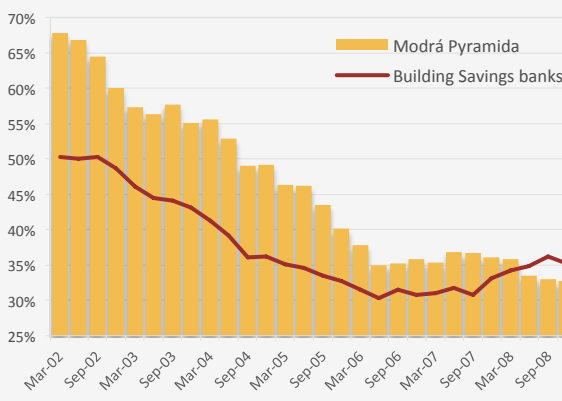
Modrá Pyramida – Key Ratios

Chart 50: Net profit



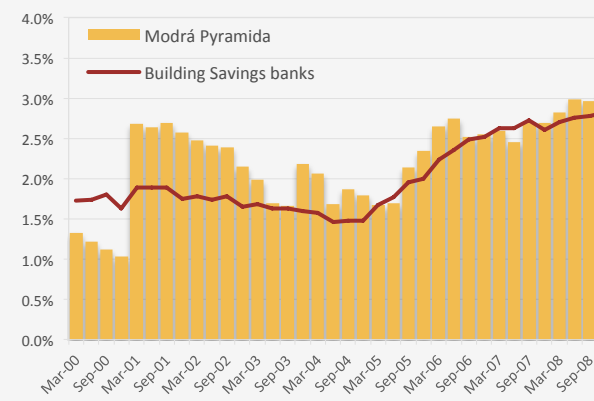
Source: Company data, Helgi Analytics

Chart 51: Cost to Income



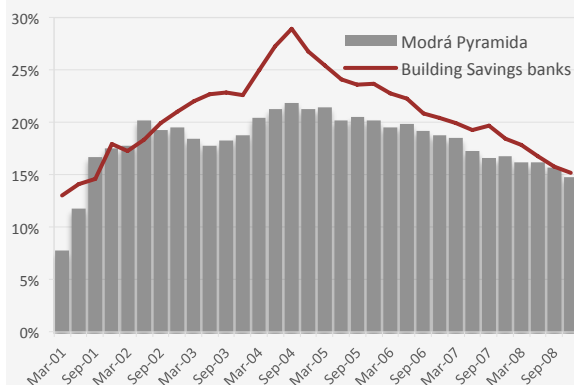
Source: Company data, Helgi Analytics

Chart 52: Asset Quality (NPL Ratio)



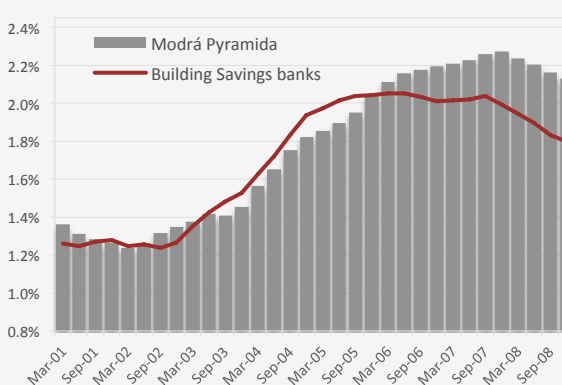
Source: Company data, Helgi Analytics

Chart 53: ROE



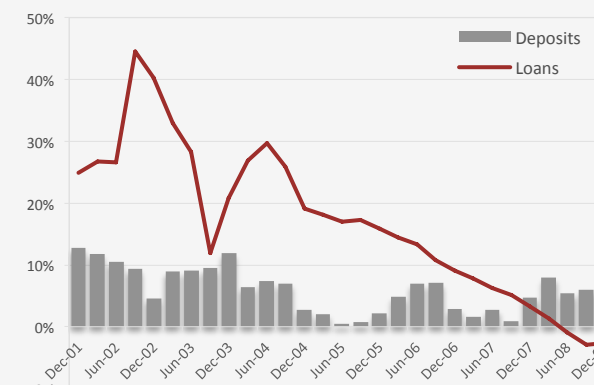
Source: Company data, Helgi Analytics

Chart 54: Net Interest Margin



Source: Company data, Helgi Analytics

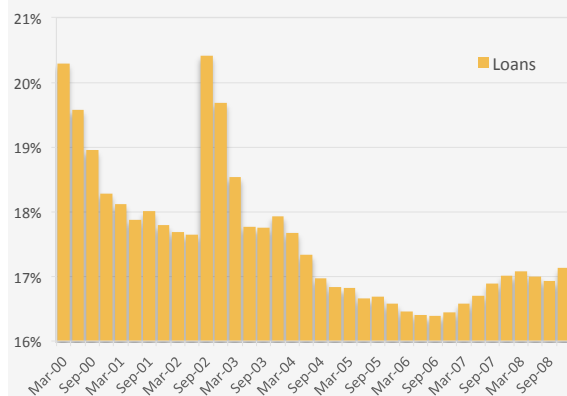
Chart 55: Loan & Deposit growth



Source: Company data, Helgi Analytics

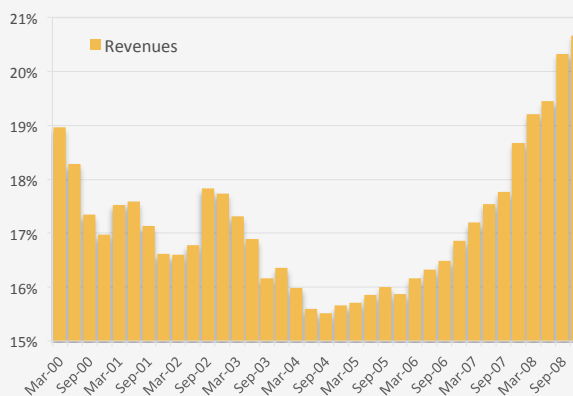
Modrá Pyramida – Market Share

Chart 56: Total loans



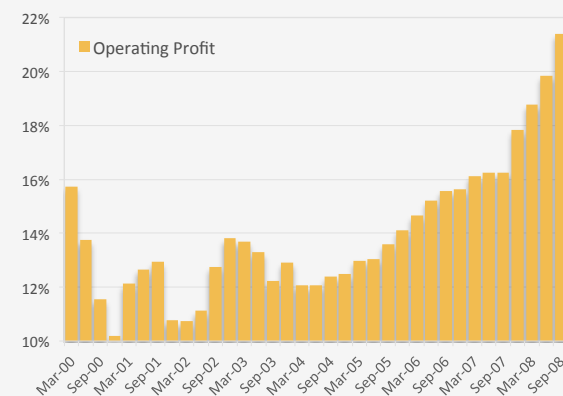
Source: Company data, Ministry of Finance, Helgi Analytics

Chart 57: Total revenues



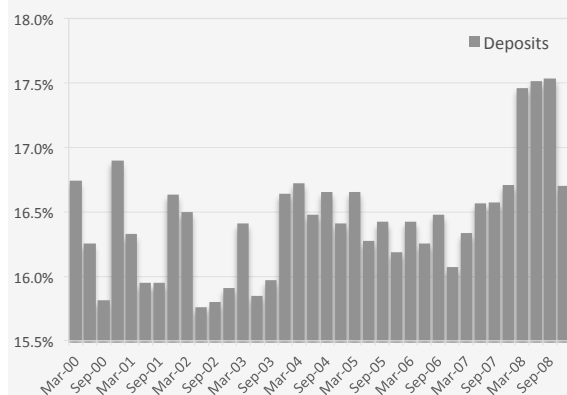
Source: Company data, Ministry of Finance, Helgi Analytics

Chart 58: Operating profit



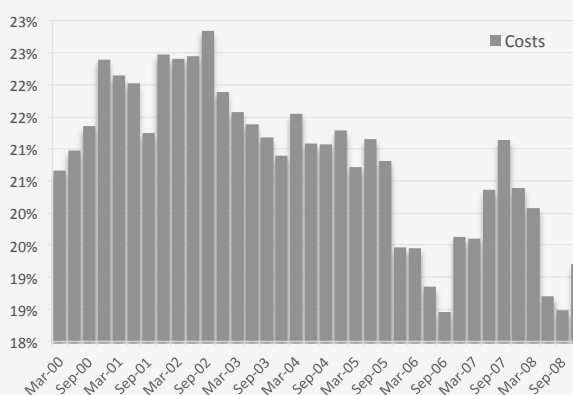
Source: Company data, Ministry of Finance, Helgi Analytics

Chart 59: Total deposits



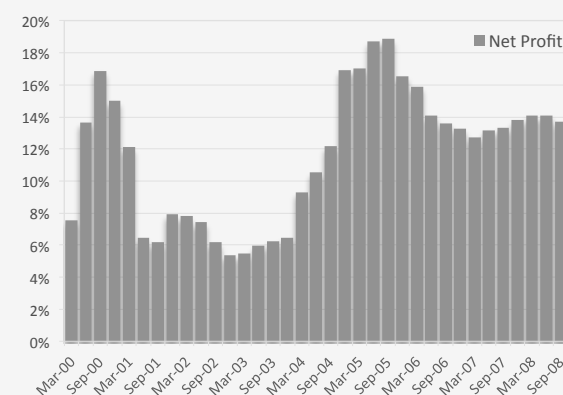
Source: Company data, Ministry of Finance, Helgi Analytics

Chart 60: Total costs



Source: Company data, Ministry of Finance, Helgi Analytics

Chart 61: Net profit



Source: Company data, Ministry of Finance, Helgi Analytics

Modrá Pyramida - Financials

Table 2: Key Figures

	4Q10	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12
Loans	49,029	49,344	49,945	50,557	50,637	50,012	49,495	49,070	48,477
Deposits	69,120	69,293	70,519	69,769	72,420	74,768	74,326	73,915	72,661
Assets	76,715	76,760	77,691	78,251	80,172	82,770	83,281	82,902	82,147
Equity	5,646	5,841	6,124	6,513	6,591	6,937	7,433	7,866	8,170
Net Interest Income	415	425	431	439	443	430	435	430	427
Non-Interest Income	40	70	45	54	56	80	73	78	79
Total Revenues	455	495	477	492	500	510	508	507	506
Operating Costs	249	351	287	329	288	367	353	350	297
Provisions	24	28	21	26	4	35	15	29	25
Net Profit	203	285	242	270	254	291	299	287	247
ROE	18.8%	18.5%	17.3%	16.6%	16.8%	16.2%	16.2%	15.7%	14.8%
ROA	1.21%	1.27%	1.26%	1.29%	1.34%	1.33%	1.37%	1.37%	1.36%
Net Interest Margin	2.14%	2.16%	2.17%	2.21%	2.22%	2.19%	2.15%	2.11%	2.08%
Asset Yield	4.57%	4.57%	4.56%	4.58%	4.54%	4.46%	4.39%	4.32%	4.28%
Cost of Funding	2.59%	2.59%	2.57%	2.57%	2.52%	2.48%	2.45%	2.42%	2.42%
Cost To Income	35.9%	35.3%	36.8%	36.6%	36.1%	35.8%	33.5%	32.9%	32.7%
Costs To Assets	0.84%	0.85%	0.90%	0.91%	0.91%	0.89%	0.83%	0.81%	0.80%
Cost Of Risk	0.22%	0.20%	0.21%	0.20%	0.16%	0.17%	0.16%	0.17%	0.21%
NPLs (As % Of Total Loans)	2.55%	2.60%	2.46%	2.70%	2.70%	2.82%	2.99%	2.97%	3.09%
Provisions (As % Of NPLs)	59.2%	59.7%	64.0%	59.4%	60.5%	60.9%	59.1%	61.8%	61.6%
Loans To Deposits	70.9%	71.2%	70.8%	72.5%	69.9%	66.9%	66.6%	66.4%	66.7%
Loans To Assets	63.9%	64.3%	64.3%	64.6%	63.2%	60.4%	59.4%	59.2%	59.0%
Capital Adequacy Ratio	13.4%	13.6%	16.4%	16.4%	16.3%	16.7%	20.1%	20.4%	20.8%
Market Share in Loans	16.4%	16.6%	16.7%	16.9%	17.0%	17.1%	17.0%	16.9%	17.1%
Market Share in Deposits	16.1%	16.3%	16.6%	16.6%	16.5%	17.0%	17.1%	17.1%	16.5%

Source: ČNB, Ministry of Finance, Association of Building Societies, Helgi Analytics, Balance sheet and Income statement figures are in CZK mil

ABOUT HELGI ANALYTICS

Helgi Analytics is a consulting company based in the Czech Republic. The company mainly provides consultancy in the area of financial services and real estate and focuses primarily on the region of Central and Eastern Europe.

Helgi Analytics also runs a web application called Helgi Library, which is a database/library offering data and analyses on more than 95% of the world's economy and population. The Library aims to bring interesting statistical data and analyses to a wide audience under affordable conditions. If you wish to get more details, please visit www.helgilibrary.com or contact us at info@helgianalytics.com.

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