

## Update to Price Target and Investment Stance

“The covid-19 pandemic has created significant instability within the global banking industry.

Apart from the pandemic related challenges, the prolonged low yielding environment has hindered the traditional banking business model and has indeed reduced the core banking profitability globally, namely in Europe, given the differential in interest rates, geographically.

Following the Bank’s latest results, we maintain our **Hold** recommendation on BOV with an updated 1-year price target of €1.05 from our previous target of €1.02.

### Updates to the valuation model:

**Net interest income (NII):** As previously anticipated, BOV’s net interest margin declined lower to circa 1.2% during FY20 (FY19: 1.3%). In view of this, we maintained our FY21 net interest income expectations (€148.3m) and extended our valuation model to FY24.

**Net fee and commission income (NFCI):** The reduction in the Bank’s NFCI throughout FY20 (-8.9%) was lower than our previous expectations (-14.3%), reflecting a pick-up in card business and economic activity in the second half of the year following the initial lockdown period.

Furthermore, the recent positive news coming from the vaccine front, and more importantly, progress in terms of the ongoing vaccination roll-out programme, augurs well for the NFCI revenue stream as we expect the volume of transactions will increase as restrictive measures will loosen. In view of this, we improved our NFCI expectations throughout our projected period.

**Operating expenditure:** Although BOV’s employee compensation and benefits were relatively close to our expectations (+11.4%), the Bank’s administrative expenses dropped by 9.1% during FY20.

As per discussions with the Bank’s executive management, BOV is currently in its final stages concerning its ongoing de-risking exercise and as such we expect BOV’s administrative expenses to stabilise moving forward. We have reflected this across our projected period.

**Net impairment losses:** In our previous coverage, we highlighted the fact that despite European banks started reversing part of their Expected Credit Losses (ECLs) provisions during 2020, we were not privy to the same moves amongst local banks. In such regard, we adopted a conservative approach and maintained our FY20 net impairment losses expectations within our valuation model (negative €15m), until we had further visibility in the near future.

**Stock Rating** **Hold**  
**Price target (1Yr)** **€1.05**

**Country** Malta  
**Industry** Banking  
**Ticker** BOV

**Price (14/04/2021)** €0.92  
**Price Target (1-Year)** €1.05  
**Upside to PT** 14.1%  
**12m cash div. (Forecast)** Nil  
**12m Total S’holder Return** 14.1%

**Market Cap** €537.1m  
**Shares Outstanding** 583.8m  
**Free Float** 64.8%

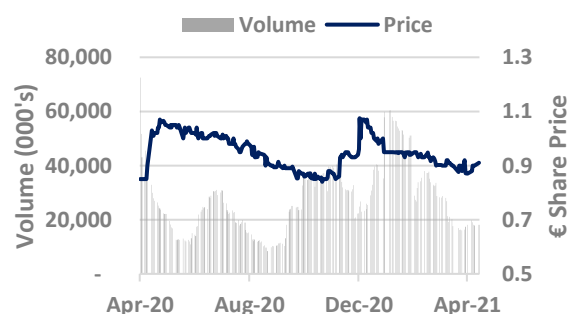
**Net Dividend Yield** Nil  
**Current P/E (FY20)** 38.9x  
**1Yr Forward P/E (FY21e)** 11.9x  
**Current P/B** 0.5x

**Group overview:** Bank of Valletta p.l.c. (“BOV” or the “Bank”) is licensed to carry out the business of banking and investment services as well to act as a tied insurance intermediary of MSV Life Assurance Company Limited.

The main companies forming part of the “Group” include Bank of Valletta p.l.c., BOV Asset Management Limited, BOV Fund Services Limited and BOV Investments Limited.

**Exchange** Malta Stock Exchange  
**52-week range** €0.84- €1.08

### Price and Volume Movement (20 day moving average)



Source: Bloomberg

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Indeed, our conservative approach proved rationale, as the Bank booked significantly higher ECLs (negative €65.1m) when compared to our estimates. BOV further reported that €38.1m of these provisions specifically relate to the implications brought about by the pandemic, whereas the remaining provisions of €39.8m relate to legacy non-performing exposures.

More constructively, in line with our underlying assumption of an improved business sentiment, especially throughout the second half of FY21, we believe that BOV should be in a brighter position to possibly be able to start reversing some of its ECLs booked during FY20. In this regard, we assuming a minor reversal of ECLs in FY21 of approximately €0.2m.

**Dividend:** In view of the significant expected credit losses booked during FY20, in addition to the fact that the Deiulementar claim is still outstanding, the Bank decided not to declare any dividend for FY20. More specifically, although BOV's CET1 ratio as at December 2020 stood at a healthy level of 20.9%, which is way above the regulatory trigger levels, we opted not to factor in a dividend payment within our valuation model for FY21. Once we have further updates concerning both the pandemic situation and the Bank's pending case, we will adjust our model accordingly.

### Concluding remarks:

BOV's financial performance was mainly characterised by an elevated negative ECLs movement of circa €65.1m, which resulted into lower profitability for the Bank on a comparative basis. Otherwise, the Bank's results are deemed to be relatively in line with our previous expectations.

In conclusion, we reiterate our stance that apart from the pandemic related issues, BOV is still facing several challenges. We are of the view that the uncertainty surrounding the Bank's pending Deiulementar case, which also impacted the bank's dividend policy, in addition to the Bank's significant growth in deposits, are key risks going forward. Furthermore, we believe that the Bank's transformation programme, and the current de-risking exercise are realistic threats for the Bank's profitability in the short-to-medium term.

On a positive note, management recently reported that positive progress has been made in terms of the Bank's ability to maintain a US dollar correspondence relationship. While stating that the Bank is very close in securing a deal with a foreign bank, management further highlighted that it is imperative for BOV to maintain US dollar transaction capabilities moving forward. In view of this, management noted that BOV is currently working on developing supplemental avenues to ensure that the Bank has the sufficient contingency measures in place to safeguard its US dollar capabilities.

Moreover, we also reiterate our stance that when considering the recent cohort efforts taken by both fiscal and monetary politicians in combating the pandemic, we believe that 2021 should be a year of normalisation. Nevertheless, moving forward, close monitoring is imperative, namely in relation to specific pandemic related events. The possible roll-out vaccine disruptions, and possibly the unprecedented new COVID-19 variants, might continue to condition the economic recovery path, and ultimately hinder the banking industry's outlook.

Furthermore, other crucial developments at an industry level include the upcoming MREL and Basel IV regulations. Given the aforementioned uncertainty we believe that a **Hold** recommendation with a 1-year price target of €1.05 on the shares of BOV is justified."

### Group Update

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- **Litigation cases:** After successfully addressing two of the historic litigation claims long outstanding against BOV, the Deiulementar claim remains outstanding and continues to be significant. In this regard, BOV reiterated its position that the curators' claim is entirely without any legal or factual basis, whereby the Bank further stated that this has been confirmed by opinions provided by independent legal experts. Moreover, the Bank further explained that it will continue to explore every legal and other proper available avenue at its disposal to bring about a change in the judicial process and deliver a fair outcome. In addition, no additional provision for litigation over the past two financial periods was taken.

## Valuation

Our 1-year price target of €1.02 is calculated using a P/B multiple of 0.6x on FY24 forecasted earnings. We substantiated our price target using the residual income method and implemented a discount rate of 14% within our valuation model.

Bank of Valletta plc for the year ended 31 <sup>st</sup> December €'000s (unless otherwise indicated)	FY18A	FY19A	FY20A	FY21F	FY22P
<b>Net Interest Income</b>	<b>156,546</b>	<b>152,850</b>	<b>146,806</b>	<b>148,324</b>	<b>150,434</b>
<b>Net fee and commission income</b>	<b>81,137</b>	<b>73,828</b>	<b>67,292</b>	<b>69,984</b>	<b>71,383</b>
Operating income	257,766	249,764	231,615	237,008	241,774
Total Operating Expenses (excl. Impairment losses/gains)	(130,598)	(163,018)	(170,382)	(175,481)	(180,536)
Net impairment losses/gains	10,816	11,562	(65,136)	195	1,801
<b>Operating Profit before Litigation provisions</b>	<b>137,984</b>	<b>98,308</b>	<b>(3,903)</b>	<b>61,722</b>	<b>63,040</b>
Litigation provisions	(75,000)	(25,000)	8,584	-	-
<b>Operating Profit</b>	<b>62,984</b>	<b>73,308</b>	<b>4,681</b>	<b>61,722</b>	<b>63,040</b>
Share of results of equity accounted investees	8,214	15,897	10,520	8,000	10,000
<b>Profit before tax</b>	<b>71,198</b>	<b>89,205</b>	<b>15,201</b>	<b>69,722</b>	<b>73,040</b>
Income tax expense	(19,788)	(25,713)	(1,399)	(24,403)	(25,564)
<b>Profit for the period</b>	<b>51,410</b>	<b>63,492</b>	<b>13,802</b>	<b>45,319</b>	<b>47,476</b>
<b>Earnings per share</b>	<b>0.09</b>	<b>0.11</b>	<b>0.02</b>	<b>0.08</b>	<b>0.08</b>

Equity Evaluation - €'000s (unless otherwise indicated)	FY18A	FY19A	FY20A	FY21F	FY22P
Equity*	994,133	1,062,305	1,077,125	1,122,444	1,155,677
Book value per share - €	1.70	1.82	1.84	1.92	1.98
Price/Book Ratio	n/a	0.51x	0.50x	0.5x	0.55x

\* Forecasted equity is calculated by aggregating the profitability with previous year closing equity, less any expected common dividend.

Ratio Analysis	FY18A	FY19A	FY20A	FY21F	FY22P
Cost Efficiency Ratio (excl. Impairment losses/gains)	50.7%	65.3%	73.6%	74.0%	74.7%
Net Interest Income Growth	7.0%	-2.4%	-4.0%	1.0%	1.4%
Net Fee and Commission Income Growth	17.5%	-9.0%	-8.9%	4.0%	2.0%
Net Operating Income Growth	7.2%	-3.1%	-7.3%	2.3%	2.0%
Growth in normalised EPS (YoY)	-46.2%	23.5%	-78.3%	228.4%	4.8%
Net Interest Margin	1.3%	1.3%	1.2%	1.2%	1.2%
Price/ Earnings Ratio	n/a	n/a	38.9x	11.9x	11.3x
CC Adjusted Earnings Yield	n/a	n/a	2.6%	8.4%	8.8%
Dividends Yield	n/a	n/a	n/a	n/a	2.7%
Dividend pay-out ratio	53.1%	n/a	n/a	n/a	30.0%

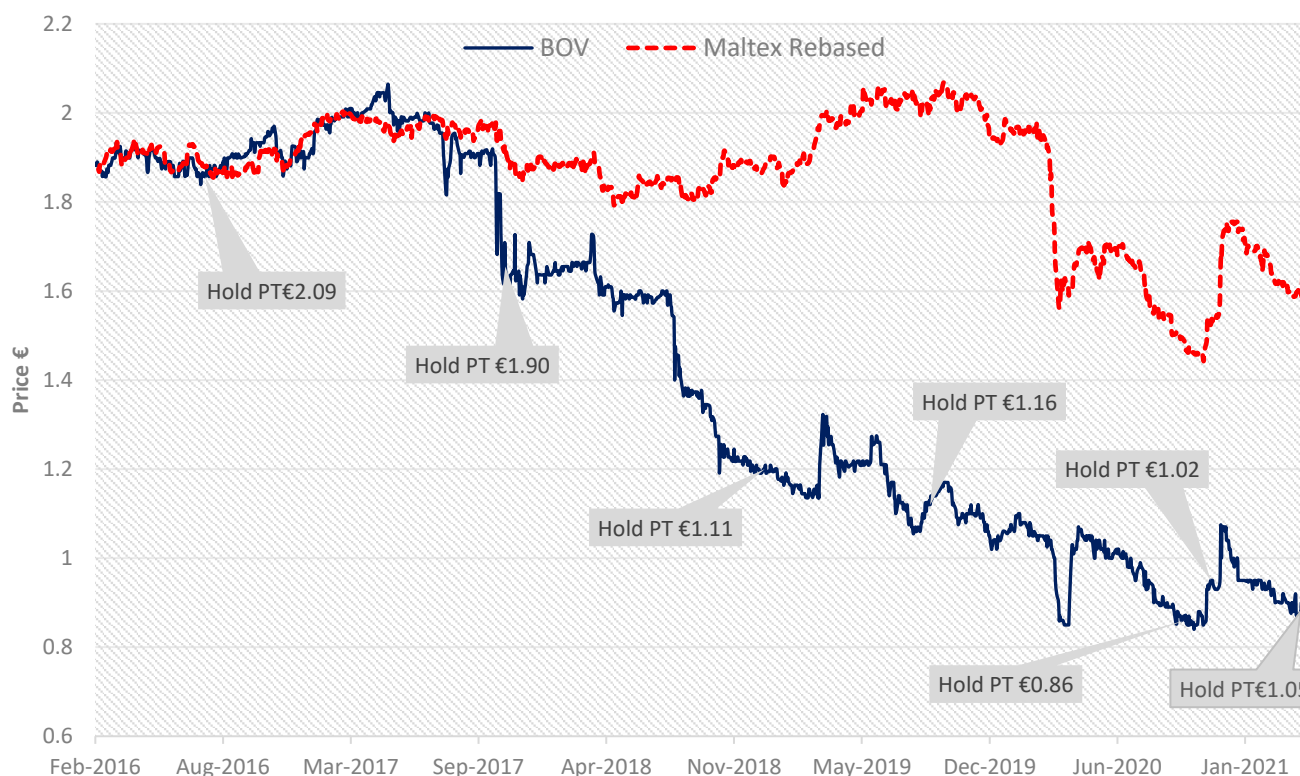
## Key Financial Indicators

Bank of Valletta plc - €'000s (unless otherwise indicated)	Dec-18	Dec-19	Dec-20
<b>Balance Sheet</b>			
Interest earning assets	11,724,784	11,836,931	12,412,045
Loans and advances to banks	490,644	501,686	479,409
Loans and advances to customers	4,498,093	4,585,234	4,867,128
Loans and advances to banks growth yoy	-6.4%	2.3%	-4.4%
Loans and advances to customers growth yoy	4.5%	1.9%	6.1%
Total deposits	10,560,929	10,695,766	11,360,320
Total deposits growth yoy	2.6%	1.3%	6.2%
Shareholders' equity	994,133	1,068,728	1,077,125
Risk weighted assets	4,673,540	4,610,703	n/a
CET1 Capital	853,389	899,388	n/a
Tier2 capital	133,016	164,472	n/a
Total capital	986,405	1,063,860	n/a
Shares Outstanding (millions)	583.8	583.8	583.8
CET1 Ratio	18.3%	19.5%	20.9%
Total Capital Ratio	21.1%	23.1%	24.5%

Source: BOV's Financial Statements and CC workings

## Historical 1-Year Price Target

Reference	Date	Price	Price Target	Analyst	Recommendation
BOV MV	15.04.2021	€0.92	€1.05	Andrew Fenech	Hold
BOV MV	11.02.2021	€0.93	€1.02	Andrew Fenech & Rowen Bonello	Hold
BOV MV	16.11.2020	€0.92	€0.86	Andrew Fenech & Rowen Bonello	Hold
BOV MV	04.09.2019	€1.13	€1.16	Simon Psaila	Hold
BOV MV	19.12.2018	€1.20	€1.11	Simon Psaila	Hold
BOV MV	08.11.2017	€1.66	€1.90	Simon Psaila	Neutral
BOV MV	26.07.2016	€1.86	€2.09	Simon Psaila	Neutral



Source: Bloomberg

## Explanation of Equity Research Ratings

**Buy:** Based on a current 12-month view of total shareholder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield), we recommend that investors buy the stock.

**Sell:** Based on a current 12-month view of total shareholder return, we recommend that investors sell the stock.

**Hold:** We take a neutral view on the stock 12-months out and, based on this time horizon, we do not recommend either a Buy or Sell. Current shareholders should consider buying on dips and selling on peaks.

Newly issued research recommendations and target prices supersede previously published research.

## Disclaimer

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## Glossary and definitions

<b>Income Statement</b>	
Net Interest income	Interest Income minus Interest Expense.
Operating Profit	Operating profit for financial services firms is the difference between operating income (revenue generation) and operating expenses (typically administrative expenses).
Profit after tax	Profit after tax is the profit made by the Group during the financial year both from its operating as well as non-operating activities.
Earnings per share ("EPS")	Earnings per share is the portion of a company's net profit allocated to each outstanding share of common stock. Earnings per share serves as an indicator of a company's profitability.
<b>Profitability and other ratios</b>	
Costs / Income ratio	It is an indicator of overall company efficiency. The ratio is calculated dividing total costs by total Operating Income.
Net interest margin	Net interest margin is the Net Interest Income for the year as percentage of average Interest-Earning assets.
Earnings yield	Earnings yield are the earnings per share for the most recent 12-month period divided by the current market price per share. Reciprocal of P/E ratio.
Dividends yield	This ratio indicates how much a Group pays out in dividends each fiscal year relative to its share price. It is computed by the dividing the Dividend per Share by the share price as at year-end.
Return on common equity	Return on common equity (ROE) measures the rate of return on the shareholders' equity of the owners of issued share capital, computed by dividing the net income by the average common equity (average equity of two years financial performance).
Return on Assets	Return on assets (ROA) is computed by dividing net income by the average total assets (average assets of two years financial performance).
<b>Balance Sheet</b>	
Interest Earnings Assets	Non-current asset are the Group's long-term investments, which full value will not be realised within the accounting year. Non-current assets are capitalised rather than expensed, meaning that the Group allocates the cost of the asset over the number of years for which the asset will be in use, instead of allocating the entire cost to the accounting year in which the asset was purchased. Such assets include intangible assets (goodwill on acquisition), investment properties, and property, plant & equipment.
Gross Loans	Gross Loans and Leases comprise Gross Loans to Customers net of Unearned Income, Allowance for Loan Losses, and other deductions from Gross Loans.
Total Deposits	Total Deposits include all customer and institutional deposits held at the Bank. They are essentially the core liabilities of banking institutions.
Shareholders' equity	Shareholders' Equity as reported by the Bank. Comprises Common Stock and Treasury Stock, Capital Surplus, Retained Earnings, Revaluations, Minority Interest and other components of Shareholders' Equity.
Risk Weighted Assets	Sum of all Risk-Weighted Assets as required for Regulatory Capital ratio measures.
Tier 1 Capital	Sum of permanent Shareholders' Equity (issued and fully paid ordinary shares/common stock and perpetual non-cumulative preference shares) and Disclosed Reserves (share premiums, retained profit, general reserves and legal reserves). In the case of consolidated accounts, this also includes minority interests in the equity of subsidiaries that are less than wholly owned. Excludes revaluation reserves and cumulative preference shares.
Total Capital	Sum of Net Tier 1 Capital and other more senior forms of capital (Tier 2 and Tier 3).
<b>Financial Strength / Capital Adequacy Ratios</b>	
Net impairment / gross loans	Net impairment gain/ (loss) on financial assets divided by gross loans.
Tier 1 ratio	Tier 1 Capital as a percentage of Risk-Weighted Assets.
Total Capital Ratio	Total Capital as a percentage of Risk-Weighted Assets.