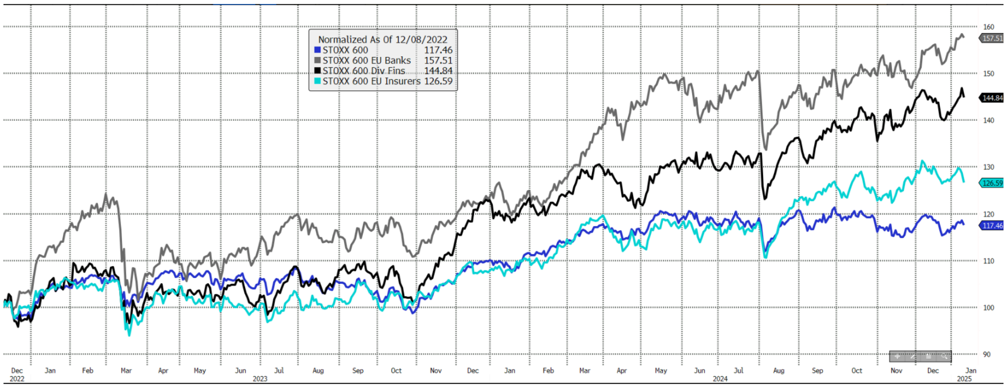
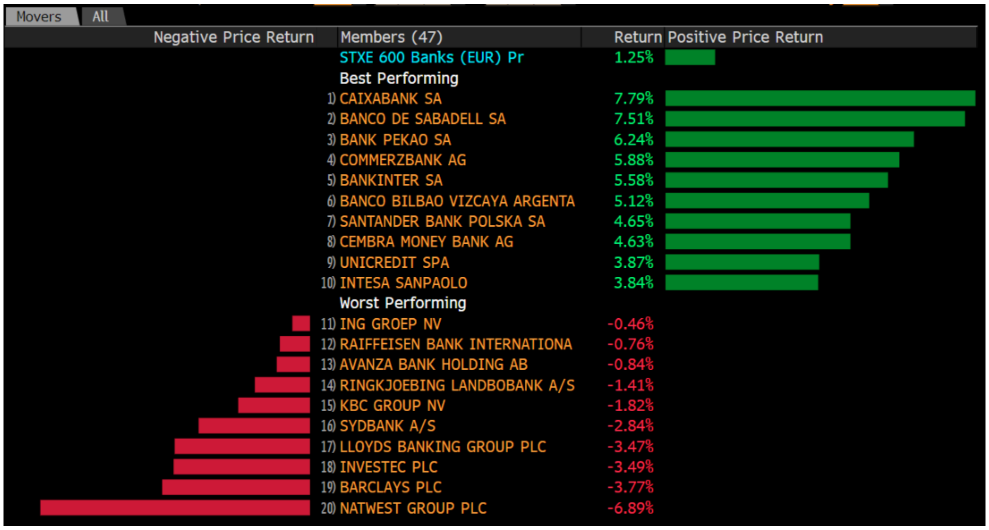
Calling Time: European Bank Snapshot 13/1/25



Spec sales: Jonathan Tyce **Jonathan Tyce**

- *European banks' **blanket outperformance is over**, we believe, as slowing growth and growing credit risk offset revenue resilience.*
- *We set out in our **What Has Changed** section how investors' thinking on how to position and use banks will shift this year*
- *Pockets of opportunity remain - e.g. **M&A, self-help measures** and **catch-up plays***
- ***Volume vs. margin is now a key debate** given recent FX moves and the impact of slower GDP growth and weakening consumer*
- ***Guidance provided on 4Q24 bank earnings** has rarely been more important, with **negative tone likely heavily punished***
- *This note aims to set out **our approach to investing in European banks** for the year ahead, with 4Q24 earnings a critical first catalyst*
- *Next week's snapshot, after US IBs report, will list key **short-term trading ideas through 4Q earnings***

Year-to-date Banks' Dispersion: *Italy-Spain 1, UK 0*



	Members (47)	Return
	STXE 600 Banks (EUR) Pr	1.25%
	Best Performing	
1)	CAIXABANK SA	7.79%
2)	BANCO DE SABADELL SA	7.51%
3)	BANK PEKAO SA	6.24%
4)	COMMERZBANK AG	5.88%
5)	BANKINTER SA	5.58%
6)	BANCO BILBAO VIZCAYA ARGENTA	5.12%
7)	SANTANDER BANK POLSKA SA	4.65%
8)	CEMBRA MONEY BANK AG	4.63%
9)	UNICREDIT SPA	3.87%
10)	INTESA SANPAOLO	3.84%
	Worst Performing	
11)	ING GROEP NV	-0.46%
12)	RAIFFEISEN BANK INTERNATIONA	-0.76%
13)	AVANZA BANK HOLDING AB	-0.84%
14)	RINGKJOEBING LANDBOBANK A/S	-1.41%
15)	KBC GROUP NV	-1.82%
16)	SYDBANK A/S	-2.84%
17)	LLOYDS BANKING GROUP PLC	-3.47%
18)	INVESTEC PLC	-3.49%
19)	BARCLAYS PLC	-3.77%
20)	NATWEST GROUP PLC	-6.89%

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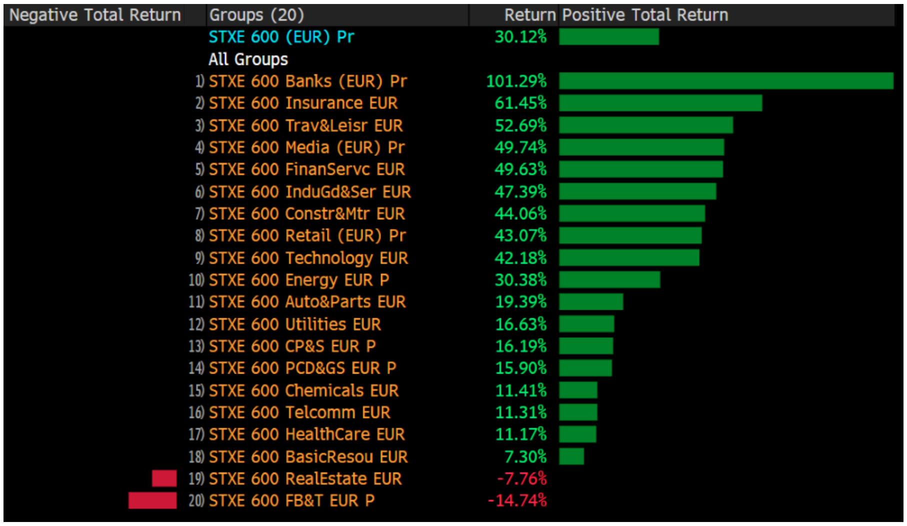
Source: Bloomberg

'Travel vs. Arrive' - Are We There Yet?

European banks' 100% total shareholder return since the first ECB rate hike in July 2022 compares with 30% for the Stoxx 600 Europe and can comfortably be justified by upgrades to revenue and EPS estimates .

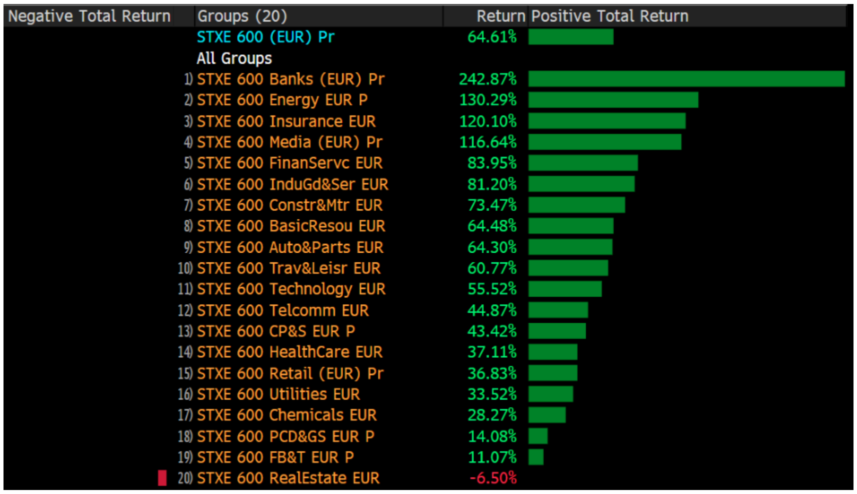
70% Outperformance Since First ECB Rate Hike



Source: Bloomberg

The sector's 180% outperformance from September 2020 lows reflected significantly greater capital return than expected and a post-Covid return to dividends as IFRS9 expected credit loss charges taken proved excessive and EPS remained resilient.

180% Outperformance From September 2020 Lows



Source: Bloomberg

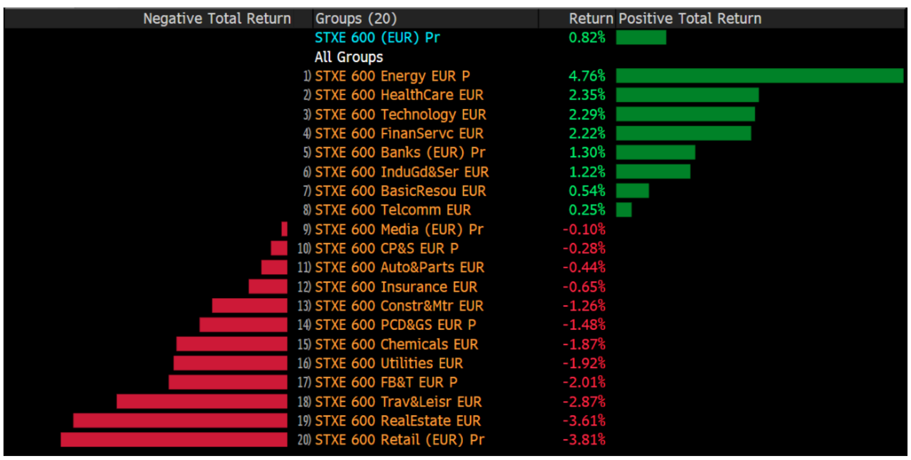
In part, this resilience was thanks to global government interventions, furlough schemes and economic support across economies that absorbed much of the pain that would have fed through as credit losses.

With policymakers' toolkits now depleted and the growing economic cost of government interest payments (as yields tick higher) limiting flexibility, banks will likely shoulder a higher real share of economic troubles ahead than post-Covid and the invasion of Ukraine.

In short, **bank earnings cannot prove as resilient to the next shock(s) as in recent years** and we believe we are now at a key inflection point described perfectly in the investing maxim *"It is better to travel than to arrive"*.

Calm Before the Storm…

YTD, Banks Still Resilient



Source: Bloomberg

Consumer weakness and downbeat guidance from European and US retailers (European retail sector down 5% relative to market YTD) so far this month are useful harbingers of a slowdown to come.

With consumer spending so critical to developed economies' GDP outlook, we are confident that the odds of recession this year across multiple geographies are rising fast.

Furthermore, higher-for-longer rates will begin to feed through to other sectors that performed well last year as the expectations for rate cuts dominated, with a ripple effect through to banks' credit quality.

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…as IFRS9 Clouds Gather

Inputs for expected credit loss calculations - as per IFRS9 - may well begin to deteriorate post-1Q, we believe. Add to this the pro-cyclical nature of IFRS 9, and the provision line for European banks could quickly turn from a source of positive earnings surprise (that the market already looks though) to a source of disappointment.

Inflation, GDP, CRE &Unemployment - ECL Risks

Updated economic scenarios

Scenario	ECL[1] (£m)	Measure (%)	2024	vs. Q2 2024	2025	2026	2027	2028	Ave. 24-28
Upside (30%)	2,806	GDP	1.2	*0.1*	2.4	1.9	1.5	1.4	1.7
		Unemployment rate	4.2	*0.1*	3.3	2.8	2.7	2.8	3.1
		HPI growth	3.5	*1.3*	4.6	7.1	6.4	5.1	5.3
		CRE price growth	1.6	*(0.6)*	9.0	4.2	1.8	0.7	3.4
		UK Bank Rate	5.06	*(0.11)*	5.08	5.16	5.34	5.58	5.24
		CPI inflation	2.6	*0.1*	2.7	2.4	2.8	2.8	2.7
Base case (30%)	3,380	GDP	1.1	*0.3*	1.3	1.5	1.5	1.5	1.4
		Unemployment rate	4.3	*(0.2)*	4.7	4.7	4.5	4.5	4.5
		HPI growth	3.1	*1.9*	2.0	1.0	1.5	2.1	2.0
		CRE price growth	0.3	*1.9*	1.7	2.1	0.7	0.3	1.0
		UK Bank Rate	5.06	*0.00*	4.19	3.63	3.50	3.50	3.98
		CPI inflation	2.6	*0.1*	2.6	2.1	2.2	2.1	2.3
Downside (30%)	4,320	GDP	1.0	*0.4*	(0.3)	0.4	1.3	1.5	0.8
		Unemployment rate	4.4	*(0.5)*	6.5	7.3	7.3	7.1	6.5
		HPI growth	2.9	*2.3*	(0.2)	(6.1)	(5.8)	(2.9)	(2.5)
		CRE price growth	(0.7)	*4.0*	(6.2)	(1.7)	(1.9)	(1.9)	(2.5)
		UK Bank Rate	5.06	*0.09*	3.11	1.48	0.96	0.65	2.25
		CPI inflation	2.6	*0.1*	2.6	1.9	1.5	1.1	2.0
Severe downside (10%)	6,865	GDP	0.9	*0.8*	(2.0)	(0.1)	1.1	1.4	0.2
		Unemployment rate	4.6	*(0.9)*	8.6	9.9	9.9	9.7	8.5
		HPI growth	2.3	*3.0*	(2.5)	(13.5)	(12.6)	(8.3)	(7.1)
		CRE price growth	(2.7)	*6.4*	(16.5)	(6.5)	(6.5)	(5.1)	(7.6)
		UK Bank Rate – adj.	5.13	*0.04*	3.67	2.55	2.16	1.88	3.08
		CPI inflation – adj.	2.6	*(0.3)*	3.5	1.8	1.3	0.9	2.0
Probability weighted	3,838								

1 – ECL excludes any impact of changes to economic scenarios in Q3.

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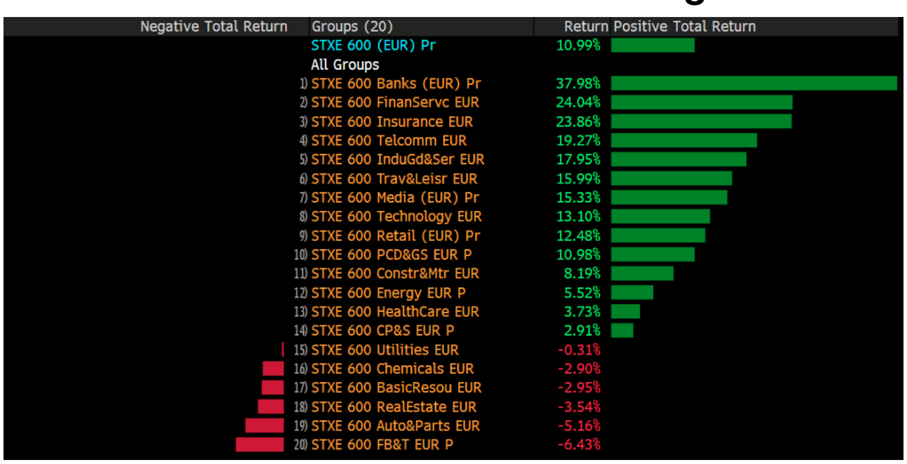
Source: Lloyds Banking Group 3Q24 IMS

Even with the cushion of management overlays (where the likes of UniCredit look relatively well positioned), market fears of rising provision charges simultaneous with falling loan growth will hit the bank sector disproportionately hard.

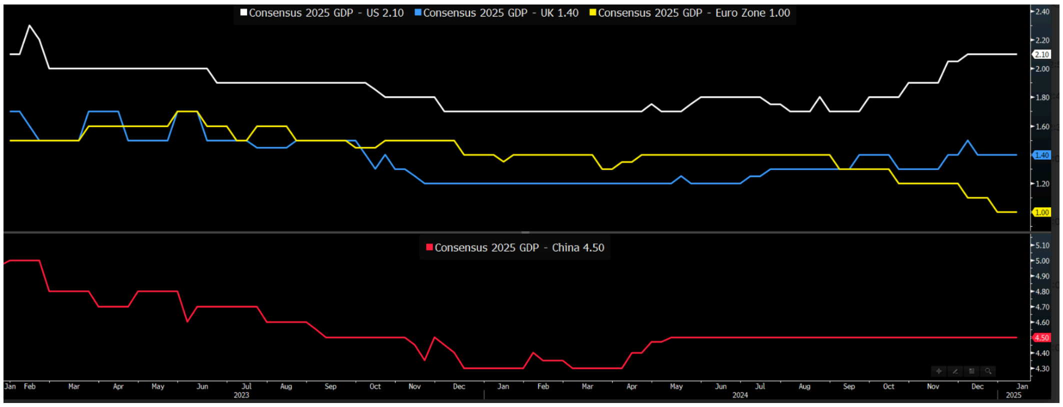
Banks' 12-Month Relative Return at Highs



Source: Bloomberg

The SX7P closed within 5% of 10-year absolute highs last week, with 17 members of the 47 stock index within 2% of 52-week highs. While we expect the banks to deliver a solid set of 4Q earnings with net interest income a bright spot and provisions remaining benign, the input drivers to ECLs are already deteriorating.

2025 GDP Forecasts - US, UK, Euro Zone, China



Source: Bloomberg

We would expect the consensus UK GDP to track euro area expectations for 2025 GDP lower, while China remains the wild card and downside looks fairly inevitable.

Return of the Inflation Monster?

Deflationary pressures in China (which we expect to intensify) may not translate directly to US and European economies, but the correlation between banks' outperformance and higher interest rates (driven by higher inflation) has now run its course, we suspect.

5Y5Y Inflation Swaps and Banks' Market Outperformance

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Inflation that drives higher loan loss charges, lower loan growth and a loss of investor sentiment and economic momentum is the perfect storm that, in our opinion, the banks now face. Stronger for longer net interest income can only partially offset this.

The good news is that dramatically improved capital positions, operational efficiency and improved management teams have positioned the banks well for this. The bad news is the market already knows this.

What's Changed? 2024 vs. 2025

The threat of recession and consumer weakness will affect many sectors beyond banks and guessing when the turn will actually occur for the sector relative is an impossible task. One thing that has clearly changed in the past 6 months, however, is how the sector will be used by investors to reflect news and positioning.

In our 7th October *Snapshot* last year - immediately ahead of 3Q earnings - we noted that moves in a number of interest-rate sensitive banks looked unfairly harsh and that the sector looked appealing again, as it had done in the immediate aftermath of the Yen-carry trade unwind in early August. We also expected that the commentary and guidance from banks would be positive in 3Q and lift shares further.

Banks No Longer the Vanguard of 'Risk On'

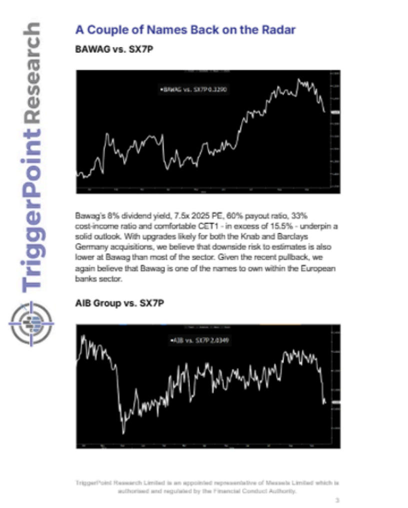
August 2024 Risk Off


European Banks *Snapshot* - 23/8/24

Spec sales: Jonathan Tyce

- *An appropriate moderation in interest rate expectations and subsequent recovery in bank stocks suggest that, as a sector,* ***very limited upside remains relative to the wider market***
- *One Savings Bank's volume and margin guidance cut are a reminder that it is better to travel than arrive and that* ***as rates fall, competition will return rapidly and margin squeeze accelerate***
- *From a revenue growth and post-2Q upgrade perspective,* ***UK and Italian banks*** *look most attractive when adjusted for valuation*
- *On 2025 multiples, the sector discounts an implied* ***cost of equity of 14.8%, PE of 7.4x and dividend yield of 7.1%*** *which looks fair*
- *YTD, SX7P now +22% TSR vs. 10% for STOXX 600, 20% for Healthcare, 14% for Insurance and +10% for Div Fins*

October 2024 Risk On


A Couple of Names Back on the Radar

BAWAG vs. SX7P

Bawag's 8% dividend yield, 7.5x 2025 PE, 60% payout ratio, 33% cost-income ratio and comfortable CET1 - in excess of 15.5% - underpin a solid outlook. With upgrades likely for both the Knab and Barclays Germany acquisitions, we believe that downside risk to estimates is also lower at Bawag than most of the sector. Given the recent pullback, we again believe that Bawag is one of the names to own within the European banks sector.

AIB Group vs. SX7P

The SX7P's near-10% outperformance since then now discounts a more positive environment for 2025 than we deem likely. Last year, underlying economic growth looked more resilient and the battle against inflation appeared nearer to an end.

While the sector is still not expensive, the trajectory and drivers of interest rates have changed. More importantly, the market's **focus on credit costs, capital buffers and capital return-capacity is on the rise and the value of stronger-for-longer interest income** in this environment - and the sector earnings multiple ascribed - **is falling**. Banks will no longer be the automatic, go-to *risk-on* play.

Sitting on the Sidelines - For Now….

Ahead of 4Q24 earnings and 2025 outlook updates, the desk prefers to sit on the sidelines for now and use managements' relative guidance and quality of 4Q results to identify key banks to own and/or avoid over the coming months.

This will also be combined with feedback from other TriggerPoint sector teams on the commentary and outlook for other sectors to refine the view on the outlook for financials versus the wider European markets. The severity and impact of new US tariffs and the turn in credit loss guidance are unlikely to be fully understood or quantified until later in 1H. That said, short-term financials trading opportunities through 4Q earnings will be the focus of next week's note, with best near-term ideas identified.

Key 2025 Themes Includes Capital Markets

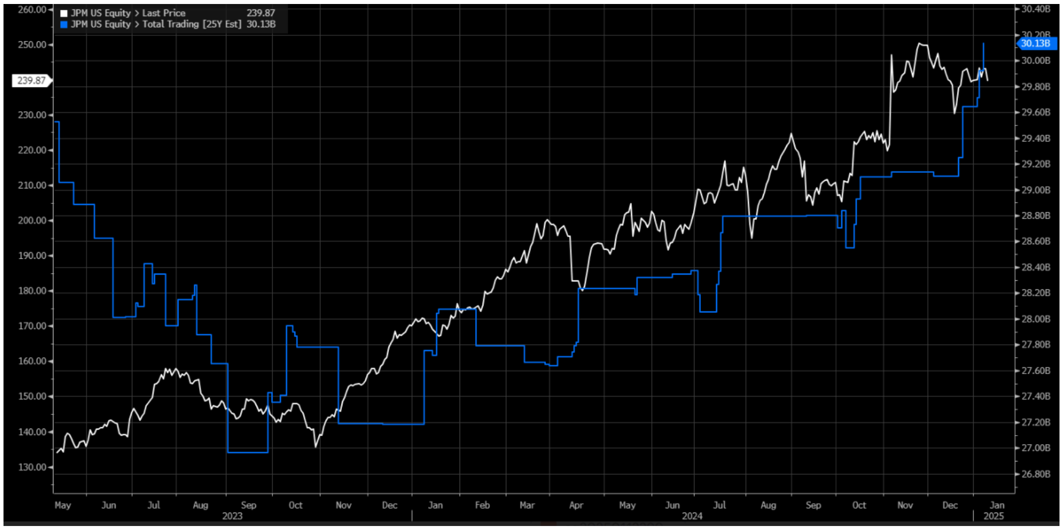
Top down, many of the critical themes that will determine relative performance this year are already well discussed. **Italian M&A; Nordic defensiveness / resilience**; and **political fallout** in **Germany, France** and the **UK's fiscal troubles** will all undoubtedly feature heavily.

Commercial and **residential property** remains a well known '*known-unknown'*, and private credit markets and liquidity therein another area to watch.

Capital markets activity - sales & trading and advisory volumes - will also be key deltas this year and as rising consensus for JPMorgan shows, expectations for a material improvement under Donald Trump's presidency are already baked in.

How this **read-across to European names** (Deutsche Bank, Barclays, BNP Paribas, UBS etc) actually plays out remains to be seen and **will determine the size of buybacks and dividends** this year.

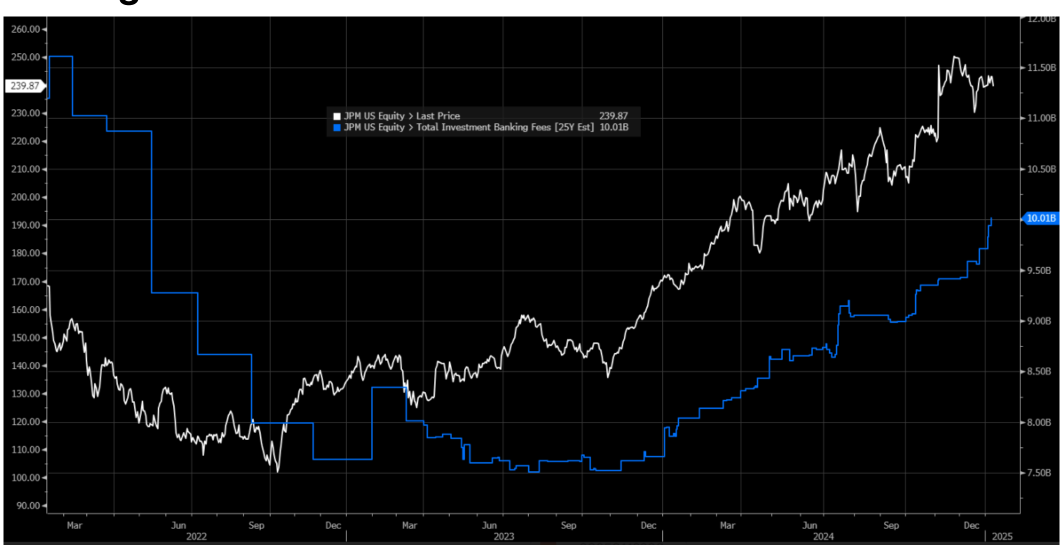
JPMorgan 2025 Consensus Trading vs. Share Price



Source: Bloomberg

JPMorgan, Goldman, Morgan Stanley, BofA and Citigroup report on the 15th and 16th January and commentary and any read-across to European wholesale funded banks versus consensus incorporated into our short-term trading ideas list.

JPMorgan 2025 Consensus IB Fees vs. Share Price



Source: Bloomberg

The Big 5 US banks are currently forecast to post an average 4Q growth of 14% year-on-year in total trading, with FICC at 11% and Equities just shy of 20%.

Equity Capital Markets (58%) and **Debt Capital Markets** fees (46%) will be most keenly watched given expectations for a huge **post-Trump spike in activity which we increasingly suspect may prove optimistic**. The desk will include updated consensus for European readacross in next week's spotlight after US reporting next week.

Performance, Valuation into Numbers

4Q Earnings Calendar, RSI and Proximity to 52-wk Highs

Exp Rep Dt	Name	52Wk High Chg Pct	RSI 14D
01/23	BANKINTER SA	-2.8%	68.261
01/23	SWEDBANK AB - A SHARES	-3.7%	61.989
01/29	SKANDINAVISKA ENSKILDA BAN-A	-6.5%	56.012
01/30	BANCO BILBAO VIZCAYA ARGENTA	-11.9%	64.352
01/30	CAIXABANK SA	-4.5%	70.859
01/30	DEUTSCHE BANK AG-REGISTERED	-1.8%	59.820
01/30	NORDEA BANK ABP	-7.7%	56.665
01/31	BANCO DE SABADELL SA	-1.6%	69.720
02/04	BNP PARIBAS	-18.8%	52.278
02/04	INTESA SANPAOLO	-3.1%	66.689
02/04	RAIFFEISEN BANK INTERNATIONA	-5.6%	54.526
02/05	CREDIT AGRICOLE SA	-16.0%	56.881
02/05	DNB BANK ASA	-3.5%	51.707
02/05	FINECOBANK SPA	-1.3%	67.423
02/05	RINGKJOEBING LANDBOBANK A/S	-6.4%	49.467
02/05	BANCO SANTANDER SA	-7.3%	55.639
02/05	SVENSKA HANDELSBANKEN-A SHS	-.9%	66.579
02/06	BANCA POPOLARE DI SONDRIO	-.5%	66.966
02/06	SOCIETE GENERALE SA	-2.7%	56.960

Source: Bloomberg

Nordic and Spanish banks are first to report 4Q earnings. Expectations for Nordic NII squeeze have been widely discussed and markets are pricing in a 100% change of a 25bps cut to 2.25% at the end of January from the Riksbank after four cuts since mid-2024.

Polish banks, Bank of Ireland and Lloyds (UK motor finance redress and UK economic outlook), BNP Paribas and Credit Agricole (French political turmoil) and NatWest rank among the banks trading furthest from 52-week highs heading into full year results.

SX7P - Banks Trading Furthest Below 52-Week Highs

Name	52Wk High Chg Pct ↑	3M Tot Ret
STXE 600 Banks (EUR) Pr	-1.1%	7%
BANK PEKAO SA	-23.5%	-3%
BANQUE CANTONALE VAUDOIS-	-23.4%	-3%
SANTANDER BANK POLSKA SA	-18.8%	3%
BNP PARIBAS	-18.8%	-5%
BANK OF IRELAND GROUP PLC	-18.5%	-4%
JYSKE BANK-REG	-17.5%	-4%
LLOYDS BANKING GROUP PLC	-16.7%	-12%
INVESTEC PLC	-16.3%	-8%
CREDIT AGRICOLE SA	-16.0%	-3%
BANCO BILBAO VIZCAYA ARGEN	-11.9%	7%
ING GROEP NV	-11.7%	-5%
NATWEST GROUP PLC	-10.8%	6%
UNICREDIT SPA	-9.4%	2%
ABN AMRO BANK NV-CVA	-7.9%	-3%
NORDEA BANK ABP	-7.7%	5%
BANCO SANTANDER SA	-7.3%	2%

Source: Bloomberg

BBVA (Mexican Peso, Sabadell deal delays) and Santander (Brazilian Real, UK weakness) are also in this club.

Currency Moves vs. Euro - 12 months

Source: Bloomberg

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Banks' PE Discount to Market Unlikely to Narrow

Source: Bloomberg

As we wrote in early December, we do not believe that there is any argument for a re-rating from here for banks versus the wider market given the proximity to a turn in the cycle and shift in focus from top line momentum to credit and operating costs.

UniCredit remains the poster child for all that has improved in the sector in recent years, with improved investor communication' material capital return; improved ROA and capital efficiency; cost-efficiency and M&A optionality all delivered in spades. Any banks that can deliver some of the above list will do well relative to the sector as 2025 unfolds


TriggerPoint Research

Banks' 50% PE Discount to Wider Market

SX7P Index / SXXP Index 0.4897

Source: Bloomberg

Still trading at a 50% discount to the wider market on forward PE, the banks look well supported. A key question is, of course, in the absence of EPS upgrade momentum that has been a key driver since early 2022, what can drive a re-rating if two years of upgrades failed to?

We remain of the opinion that a material re-rating is unlikely as tailwinds become headwinds for the sector, but as the UniCredit story shows, a re-rating is not required for material outperformance.

UniCredit Case Study

UniCredit's 2022-24 Consensus EPS History

Source: Bloomberg

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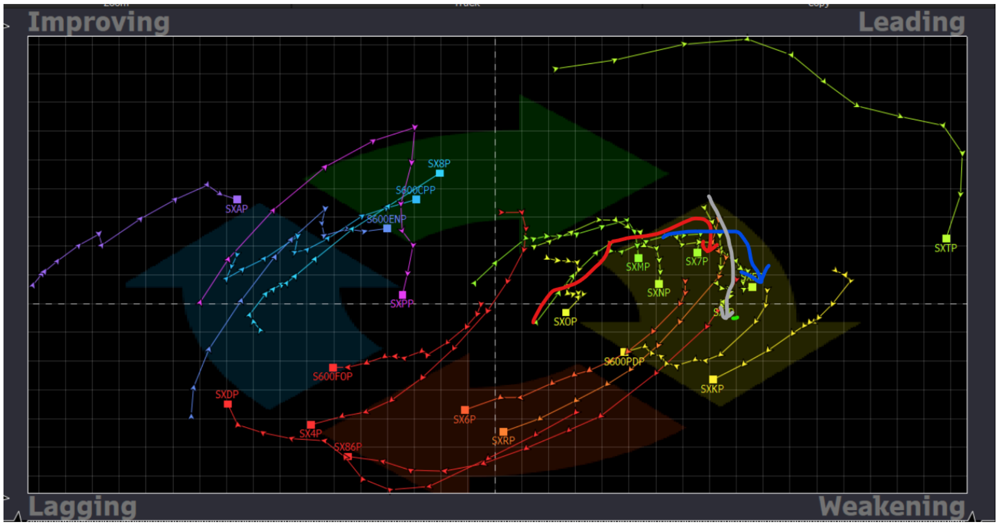
Source: TriggerPoint Spec Sales Not, December 12, 2024

Sector Positioning....Neutral

Insurers Now Screen Least Well of Financials



Source: Bloomberg RRG Function

The tight spread of sector momentum currently demonstrates a lack of conviction and growing fears in the market. Technology, Basic resources and autos are trending most positively as mean reversion and market catch up takes hold. The SXIP's **(grey arrow)** nosedive is as much due to the impact of Californian wildfires as more fundamental concerns, we suspect, with Banks **(red arrow)** and Diversified financials **(blue arrow)** looking fairly neutral.

Banks Looking Good at the Start of November

Source: Bloomberg RRG Function

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Compared to relative sector momentum immediately after 3Q earnings and just prior to Donald Trump's victory, the major trend is the number of sectors that are now weakening.

Banks, Insurers Screened Poorly 1-year Ago

Source: Bloomberg RRG Function

We would also highlight that heading into full year earnings last year, banks and insurers screened poorly but stronger outlooks, better revenues and higher capital return returned them to the top of investors' rankings quickly. The scale of consensus beats from the banks for 4Q24 is likely far more limited than last year but, if mildly positive (as we expect) could defer the timing and pace of rotation out of the sector.

Valuation - Groundhog Day

On most metrics, the SX7P screens fairly with implied cost of equity well below recent highs and an average 2025 PE just shy of 8x neither cheap nor expensive.

The **usual suspects screen inexpensively** - from Societe Generale and Deutsche Bank to Barclays and BNP - while the names considered more defensive - Nordics, KBC, UBS - screen most inexpensively. In short, ***the order of things has remained largely unchanged throughout the last few years despite a significant rally***.

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UniCredit has rather earned its spurs and no longer ranks as one of the cheapest while BNP has lost its mojo somewhat in the eyes of the market and de-rated.

2025 Implied COE of 13.6% is Towards Bottom of Range

Name	Implied CoE (%) FY1	Implied CoE (%) FY2↓	Implied CoE (%) FY3
Median	13.44	12.95	13.87
Average	13.75	13.60	14.63
Raiffeisen Bank Internatio…	30.63	28.97	28.00
Societe Generale SA	15.73	18.63	22.71
Deutsche Bank AG	12.35	17.73	19.84
Banco Santander SA	16.00	17.01	17.83
BNP Paribas SA	16.21	16.80	18.84
Bank of Ireland Group PLC	18.48	16.52	16.22
Barclays PLC	13.52	15.97	18.02
Banco Bilbao Vizcaya Arge…	17.41	15.68	15.90
Credit Agricole SA	15.68	15.68	16.75
UniCredit SpA	14.60	15.62	16.78
ABN AMRO Bank NV	17.76	15.51	16.72
NatWest Group PLC	13.81	14.88	16.39

Source: Bloomberg

The path of ECB rate cuts is now one of the biggest unknowns, with a January and March cut priced in by money markets. Again, **we prefer a wait-and-see approach** given that the **impact of any tariffs** imposed on Europe and globally by the incoming President is a critical factor..

Usual Suspects Screen Cheaply / Expensively

Name	Implied CoE (%) FY1	Implied CoE (%) FY2↑	Implied CoE (%) FY3
Median	13.41	13.04	15.79
Average	13.33	13.53	14.92
UBS Group AG	5.15	7.07	10.50
Svenska Handelsbanken …	11.41	9.52	9.41
Skandinaviska Enskilda B…	11.51	10.12	10.76
KBC Group NV	10.74	10.59	11.70
DNB Bank ASA	12.11	10.95	10.99
Swedbank AB	13.47	11.63	11.68
Lloyds Banking Group PLC	12.66	12.13	15.92
Erste Group Bank AG	12.88	12.28	12.64
CaixaBank SA	13.49	12.47	12.66
Danske Bank A/S	13.11	12.50	12.83
Intesa Sanpaolo SpA	11.90	12.59	12.91
Nordea Bank Abp	13.57	12.74	12.98

Source: Bloomberg

6-7% Dividend Yield Supportive, Little More

Name	Div Yield FY1 (%)	Div Yield FY2 (%)↓	Div Yield FY3 (%)
Median	7.25	7.14	7.50
Average	6.74	6.69	7.03
Intesa Sanpaolo SpA	8.35	8.90	9.15
Svenska Handelsbanken …	10.36	8.75	8.16
Nordea Bank Abp	8.80	8.74	8.85
Banco BPM SpA	9.96	8.51	8.52
BNP Paribas SA	7.94	8.40	9.30
Mediobanca Banca di Cr…	7.75	8.32	8.65
Komercni Banka AS	9.78	8.10	6.75
Credit Agricole SA	7.91	8.07	8.50
Banco de Sabadell SA	8.33	8.03	7.09
Danske Bank A/S	10.73	7.88	7.86
Swedbank AB	7.25	7.87	8.32
Raiffeisen Bank Internat…	6.77	7.81	8.64

Source: Bloomberg

Capital return remains an important differentiating factor between banks, with buybacks key to maintaining EPS momentum as revenue stalls and its significance flagging management visibility and relationships with regulators. Here we would expect positive newsflow to continue.

Name	BEst P/E Nxt Yr ↑	Dvd Est Yld	BEst EPS 4Wk % Chg
BANCO SANTANDER SA	5.8	4.6	-1.0%
BNP PARIBAS	6.0	7.9	.0%
DEUTSCHE BANK AG-REGISTERE	6.2	3.8	.0%
BANK PEKAO SA	6.3	11.9	1.5%
INVESTEC PLC	6.4	7.0	.0%
BANK OF IRELAND GROUP PLC	6.4	7.6	.4%
BARCLAYS PLC	6.4	3.3	.7%
BANCO BILBAO VIZCAYA ARGEN	6.5	8.0	.6%
CREDIT AGRICOLE SA	6.6	7.9	.1%
UNICREDIT SPA	6.6	6.0	-.3%
PKO BANK POLSKI SA	6.6	7.1	2.5%
ABN AMRO BANK NV-CVA	6.7	9.0	-.6%
STANDARD CHARTERED PLC	6.8	2.6	1.0%
NATWEST GROUP PLC	7.0	5.2	.6%
BPER BANCA SPA	7.0	10.0	.0%
BANCO DE SABADELL SA	7.1	8.3	.4%
JYSKE BANK-REG	7.2	5.0	-1.0%
LLOYDS BANKING GROUP PLC	7.4	5.9	-1.4%
ING GROEP NV	7.5	7.4	.4%
COMMERZBANK AG	7.6	3.1	-.3%

Source: Bloomberg

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