

### Inexpensive but...

#### Downgrade to Underperform, TP up to PLN36.0 from PLN35.0

KNF ban on 2022 dividend came as a negative surprise to us. It reminded us that PKO skips dividend payments more often than not. PKO certainly seems inexpensive on P/E ratio, but not necessarily if one is looking at P/BV or DY.

Newsflow wise we see mostly risks for PKO. We are ahead of a finish of tight parliamentary election campaign and ahead of first rate cut (PLN FRA reflects 100bp cut in 2023 and further 175bp cut in 2024; Brazil cut 50 bps in Aug'23, Chile cut 100bps in Jul'23).

**Not a dividend payer.** End of July KNF banned 2022 dividend from PKO and said no to PKO paying PLN1.6bn. Multiple reasons were cited: CHF portfolio, inflation, GDP outlook, debt servicing cost, concerns on stability of the bank and further development of the bank. In the last 10 years PKO paid dividend only 4 times for the total consideration of PLN5.6bn (18% payout). This allowed to build massive capital buffer over minimum requirements of PLN17.8bn (PKO reported CET1 of 18.75% vs regulatory minimum of 10.53%). Next year will be interesting as PKO is likely to meet KNF requirements allowing PKO to pay 100% of 2023 net income in dividend. We are sceptical of such high pay-out and assume 50% pay-out implying 6.6% dividend yield.

#### (Too?) generous 10% deposit offer attracts PLN4bn and 20k clients.

On June 1<sup>st</sup> PKO launched [promotional offer](#) 6-month term deposit paying 10%. The offer was terminated after having attracted PLN4bn of deposits that could cost PKO up to PLN200mn or PLN1k per attracted client. We were surprised to see such an offer in an environment of banks reducing deposit prices. We assume PKO offering was equally attractive in other segments. Owing to 6% q/q growth PKO gained visible market share in deposits (market was +1%).

**Cost of hedging was at PLN1,078mn in Q23 and totalled PLN4,689mn for the last 12 months...** As expected, this cost declined for the second quarter in a row and is expected to further decline.

**Cost of risk should remain low...** as we read positive CRO comments on outlook and notice further increase in Stage2 coverage to above 12% (vs 6% 2 years ago).

**Valuation and risk.** We set our Dec'24 TP at PLN36.0 that is a weighted average of DDM pointing to a valuation of PLN36.7 and a comparative valuation pointing to PLN37.1 (all per share) reduced by PLN 1 related to the anticipated further cost of the CHF portfolio. We note risks related to governance, macro, regulations, CHF-mortgages, dividends and equity flows.

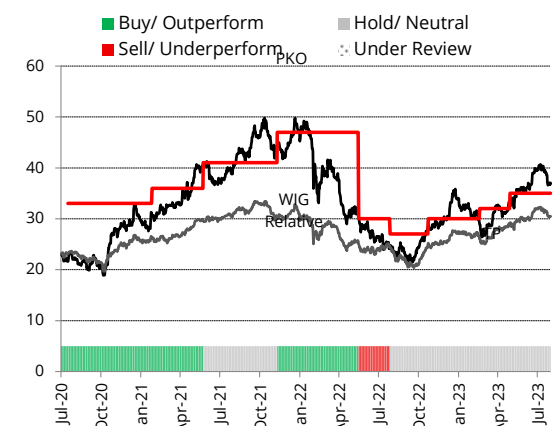
**Fig. 1. PKO BP: Financial summary**

PLNmn	2021	2022	2023E	2024E	2025E
P/E (adjusted)	11.2x	4.6x	4.9x	5.7x	6.4x
P/E (reported)	11.2x	11.4x	7.6x	6.3x	6.4x
P/BV	1.45x	1.07x	1.07x	0.98x	0.91x
Dividend Yield	6.0%	0.0%	6.6%	8.0%	7.8%
EPS (PLN)	3.90	6.59	7.56	6.53	5.82
DPS (PLN)	1.83	0.00	2.46	2.98	2.91
BVPS (PLN)	30.2	28.4	34.8	38.3	41.2
Net Income (adj. PLN mn)	4,874	8,240	9,452	8,169	7,270
Net Income (PLN mn)	4,874	3,333	6,145	7,440	7,270

Source: Company data, Santander Brokerage Poland estimates

Recommendation	Underperform
Dec'24 Target Price (PLN)	36.0

Current price (PLN, 24 Aug 2023)	37.40
Market cap. (PLNbn)	46.8
Avg. daily turnover (PLNmn)	77.0
Number of shares (mn)	1,250



The chart measures performance against the WIG index.

Main shareholders	% of votes
Republic of Poland Ministry of State Treasury	29.43%
NN OFE	8.66%
Allianz OFE	8.33%

Source: Stooq.pl, Santander Brokerage Poland

#### Analyst

**Kamil Stolarski, PhD, CFA,**  
head of Equity Research  
Equity Analyst

+48 22 586 100 kamil.stolarski@santander.pl

Fig. 2. Valuation summary (PLN/share)

Recommendation	Underperform	DDM valuation (PLN/share)	36.7	Comp. Valuation PLN/share	37.1
Dec'24 Target Price (PLN)	36.00	Discounted dividends (PLN/share)	10.2	Net Income (PLN mn, next 12 months)	9,278
Current price (PLN)	37.40	Terminal value (PLN/share)	26	Applied P/E (x)	5.0
Prospective upside (%)	-4	Terminal ROE (%)	14.62	P/E peers (x)	6.0
<i>*Our Target Price is calculated as rounded average of DDM Valuation (50% weight) and Comp (50% weight) less estimated impact of CHF- mortgages.</i>		g (%)	3.00	<b>CHF impact</b> <b>-1.0</b>	
		CoE (%)	13.80		
		RFR (%)	12.80		
		Beta (x)	1.30		
		ERP (%)	6.0		

Fig. 3. DDM Valuation sensitivity (PLN/share)

ROE->	10.6%	12.6%	14.6%	16.6%	18.6%
1.0%	28.4	32.2	36.0	39.8	43.5
2.0%	28.0	32.2	36.3	40.4	44.5
3.0%	27.6	32.1	36.7	41.2	45.8
4.0%	27.0	32.1	37.1	42.2	47.3
5.0%	26.3	32.0	37.7	43.5	49.2

Fig. 4. DDM Valuation sensitivity (PLN/share)

ERP->	4.0%	5.0%	6.0%	7.0%	8.0%
4.0%	58.6	48.2	40.9	35.7	31.7
4.5%	54.1	45.1	38.7	34.0	30.3
5.0%	50.2	42.3	36.7	32.4	29.1
5.5%	46.8	39.9	34.9	31.0	28.0
6.0%	43.8	37.8	33.2	29.8	27.0

Fig. 5. Our forecast vs Bloomberg consensus

	Bloomberg consensus			Our assumptions vs cons.		
	2023E	2024E	2025E	2023E	2024E	2025E
Net income	5,761	6,614	6,824	%	12%	7%
DPS (PLN)	2.43	3.06	2.99	1%	-3%	-3%
ROE (%)	13.3	14.7	14.3	2 pp	2 pp	0 pp

Fig. 6. Comps Valuation sensitivity (PLN/share)

Fair P/E (x)	1.0x	2.0x	3.0x	5.0x	8.0x	12.0x
vs. peers (%)	-81	-62	-42	-4	54	131
Sensitivity	7.4	14.8	22.3	37.1	59.4	89.1

Fig. 7. Ratios, Assumptions and Forecasts

P&L (PLN mn)	2021	2022	2023E	2024E	2025E
NII	9,882	14,924	17,405	16,175	15,393
F&C	4,431	4,951	4,735	4,853	4,975
Trading Income	718	310	177	194	192
Total Revenue	15,079	20,383	22,481	21,382	20,721
Cost	-6,174	-7,850	-7,376	-7,781	-8,159
NLLP	-1,345	-1,564	-1,338	-1,542	-1,583
one-offs	0	-5,025	-4,041	-900	0
Pre-tax Profit	7,591	6,015	9,788	11,199	11,018
Banking tax	-1,079	-1,266	-1,248	-1,296	-1,324
<b>Net Income</b>	<b>4,874</b>	<b>3,333</b>	<b>6,145</b>	<b>7,440</b>	<b>7,270</b>
Net Income (adj.)	4,874	8,240	9,452	8,169	7,270

PLN bn	2021	2022	2023E	2024E	2025E
Total Assets	420	431	472	485	496
Bonds	135	136	169	176	183
Loans	236	232	242	247	252
Loans growth (%)	6	-2	4	2	2
Deposits	322	340	375	383	391
Equity	38	35	44	48	52
Mortgage loans	115	105	107	110	113
CHF mortgages	20	17	13	10	8
Other retail loans	31	32	34	36	37
Corporate loans	92	104	104	106	108

NIM ratios (%)	2021	2022	2023E	2024E	2025E
Asset yield (%)	2.82	4.97	6.37	5.18	4.78
Funding cost (%)	0.22	1.41	2.55	1.79	1.65
NIM (%)	2.64	3.77	4.15	3.64	3.37

Risk ratios (%)	2021	2022	2023E	2024E	2025E
Stage 3 ratio (%)	3.9	3.7	3.7	3.7	3.7
Stage 3 coverage (%)	61.3	61.8	61.1	61.1	61.1
Cost of risk (%)	0.59	0.67	0.57	0.63	0.63

Du Pont (%)	2021	2022	2023E	2024E	2025E
NII/assets	2.48	3.51	3.86	3.38	3.14
CoR/assets	-0.34	-0.37	-0.30	-0.32	-0.32
F&C/assets	1.11	1.16	1.05	1.01	1.01
Other rev/assets	0.20	0.14	0.09	0.08	0.08
Costs/assets	-1.55	-1.85	-1.63	-1.63	-1.66
Taxes&other/assets	-0.68	-1.81	-1.70	-0.97	-0.76
ROA	1.22	0.78	1.36	1.56	1.48
Leverage (x)	10.3	11.6	11.4	10.5	9.9
ROE (reported)	12.55	9.11	15.56	16.27	14.62

Capital & dividends	2021	2022	2023E	2024E	2025E
Tier-1 (PLN bn)	38.2	40.8	44.1	47.2	50.9
Tier-2 (PLN bn)	2.7	2.7	2.7	2.7	2.7
TCR (PLN bn)	17.5	17.2	18.0	18.4	18.8
RWA (PLN mn)	202.9	199.1	207.8	212.3	216.9
CT1 ratio (%)	17.4	18.9	19.6	20.6	21.7
CAR ratio (%)	18.6	20.2	20.8	21.7	22.9
Div. payout (%)	46.9	0.0	50.0	50.0	50.0
Dividend (PLN mn)	0	2,288	0	3,072	3,720
No. of shares (mn)	1,250	1,250	1,250	1,250	1,250

Source for all tables: Company data, Bloomberg, Santander Brokerage Poland estimates

NOTE: historical valuation ratios based on eoy prices.

## Quarterly Earnings summary

Excluding CHF provisions 2Q23 net income would be at PLN3,061mn, 1% higher than we expected.

PKO BP reported 2Q23 net income of PLN587mn; 20% higher than consensus of PLN490mn, driven by:

- CHF provisions stood at PLN2,474mn vs PLN2.5bn mentioned in the profit warning;
- NII came 2% higher than consensus. 5% q/q growth of NII is the market average;
- OpEx was 2% higher than expected;
- NLLP surprised positively;
- Tax rate was higher than we expected

**Fig. 8. Results review (year to December)**

PKO BP (PLN mn)	2Q22	3Q22	4Q22	1Q23	2Q23	q/q	y/y	2Q23E	vs. E	cons.	vs. cons.
Net Interest Income	3,639	3,927	4,158	4,187	4,392	5	21	4,322	2	4,302	2
Fees & commissions	1,249	1,282	1,241	1,269	1,298	2	4	1,282	1		
Trading Income	14	150	66	56	23	-59	64	49	-53		
Other (Net)	52	55	41	20	65	225	25	40	63		
<b>Total Revenue</b>	<b>4,954</b>	<b>5,414</b>	<b>5,506</b>	<b>5,532</b>	<b>5,778</b>	<b>4</b>	<b>17</b>	<b>5,693</b>	<b>1</b>	5,704	<b>1</b>
Personnel Costs	-854	-851	-947	-942	-989	5	16	-970	2		
General Expenses	-1,249	-780	-538	-786	-494	-37	-60	-480	3		
D&A	-256	-260	-267	-257	-263	2	3	-266	-1		
<b>Operating Expenses</b>	<b>-2,359</b>	<b>-1,891</b>	<b>-1,752</b>	<b>-1,985</b>	<b>-1,746</b>	<b>-12</b>	<b>-26</b>	<b>-1,716</b>	<b>2</b>	<b>-1,735</b>	<b>1</b>
<b>Operating Income</b>	<b>2,595</b>	<b>3,523</b>	<b>3,754</b>	<b>3,547</b>	<b>4,032</b>	<b>14</b>	<b>55</b>	<b>3,977</b>	<b>1</b>		
Net Loan Loss Provisions	-226	-460	-374	-339	-226	-33	0	-250	-10	-273	-17
Other (Net)	-1,176	-3,111	-738	-967	-2,474	156	110	-2,500	-1	-2,500	-1
Associate income	14	33	10	23	13	-43	-7	10	30		
<b>Pre-tax Profit</b>	<b>1,207</b>	<b>-15</b>	<b>2,652</b>	<b>2,264</b>	<b>1,345</b>	<b>-41</b>	<b>11</b>	<b>1,237</b>	<b>9</b>		
Corporate Income Tax	-466	105	-604	-512	-445	-13	-5	-400	11		
Minority interests	0	1	-2	1	-2			0			
Banking tax'	-319	-328	-312	-299	-311	4	-3	-307	1		
<b>Net Income</b>	<b>422</b>	<b>-237</b>	<b>1,732</b>	<b>1,454</b>	<b>587</b>	<b>-60</b>	<b>39</b>	<b>530</b>	<b>11</b>	<b>490</b>	<b>20</b>
NI excl. one-offs	2,195	2,377	2,252	2,421	3,061	26	39	3,030	1		

Balance Sheet (PLN bn)	2Q22	3Q22	4Q22	1Q23	2Q23E	q/q	y/y	2Q23E	vs. E
Net client lending	234.6	235.0	231.7	237.5	236.1	-1	1	237.5	-1
Bonds	129.6	129.4	135.6	146.0	163.5	12	26	146.0	12
Customer deposits	326.3	340.4	339.6	349.7	366.1	5	12	349.7	5
Total assets	428.8	438.5	430.7	444.0	460.8	4	7	454.0	1
Equity ex minorities	31.0	31.7	35.4	39.3	41.1	5	33	41.4	-1

Key Ratios (%)	2Q22	3Q22	4Q22	1Q23	2Q23E	q/q	y/y	2Q23E	vs. E
Net Interest Margin	3.73	3.97	4.16	4.13	4.15	2 bp	148 bps	4.15	0 bp
Cost to Income	-48	-35	-32	-36	-30	6 pp	17 pp	-30	0 pp
Cost of risk [bps]	-38	-78	-64	-58	-42	16 bp	-3 bps	-42	0 bp
Loans to deposits ratio	72	69	68	68	68	0 pp	-4 pp	68	0 pp
ROE	5.1	-3.0	20.6	15.6	5.3	-10.2 pp	0.3 pp	5.3	0.0 pp

Source: Company data, Santander Brokerage Poland estimates.

## Forecast changes

**Fig. 9. PKO – Forecast changes – P&L**

P&L (PLN mn)	2023E				2024E				2025E			
	New	Old	%	PLN mn	New	Old	%	PLN mn	New	Old	%	PLN mn
NII	17,405	17,133	2	272	16,175	15,694	3	481	15,393	14,947	3	446
F&C	4,735	4,907	-4	-172	4,853	5,029	-3	-176	4,975	5,155	-3	-180
Trading Income	177	202	-13	-26	194	194	0	0	192	192	0	0
Total Revenue	22,481	22,383	0	99	21,382	21,077	1	305	20,721	20,454	1	267
Cost	-7,376	-7,346	0	-30	-7,781	-7,750	0	-31	-8,159	-8,126	0	-33
NLLP	-1,338	-1,553	-14	215	-1,542	-1,566	-2	24	-1,583	-1,608	-2	24
One-offs	-4,041	-5,217	-23	1,176	-900	-3,000		2,100	0	0		0
Pre-tax Profit	9,788	8,319	18	1,469	11,199	8,801	27	2,398	11,018	10,760	2	258
Banking tax	-1,248	-1,217	2	-30	-1,296	-1,244	4	-52	-1,324	-1,273	4	-51
Net Income	6,145	5,222	18	923	7,440	5,621	32	1,818	7,270	7,120	2	150
Net Income (adj.)	9,452	9,630	-2	-178	8,169	8,051	1	117	7,270	7,120	2	150

NIM ratios (%)	New	Old	%	New	Old	%	New	Old	%
Asset yield (%)	6.37	6.30	0.07	5.18	5.11	0.07	4.78	4.71	0.07
Funding cost (%)	2.55	2.47	0.09	1.79	1.69	0.10	1.65	1.55	0.10
NIM (%)	4.15	4.17	-0.01	3.64	3.66	-0.02	3.37	3.39	-0.02

Du Pont (%)	New	Old	%	New	Old	%	New	Old	%
NII/assets	3.86	3.87	-0.01	3.38	3.40	-0.02	3.14	3.15	-0.02
CoR/assets	-0.30	-0.35	0.05	-0.32	-0.34	0.02	-0.32	-0.34	0.02
F&C/assets	1.05	1.11	-0.06	1.01	1.09	-0.07	1.01	1.09	-0.07
Other rev/assets	0.09	0.09	0.00	0.08	0.09	0.00	0.08	0.08	0.00
Costs/assets	-1.63	-1.66	0.02	-1.63	-1.68	0.05	-1.66	-1.72	0.05
Taxes&other/assets	-1.70	-1.88	0.17	-0.97	-1.34	0.36	-0.76	-0.77	0.00
ROA	1.36	1.18	0.18	1.56	1.22	0.34	1.48	1.50	-0.02
Leverage (x)	11.4	11.3	0.1	10.5	10.2	0.2	9.9	9.7	0.2
ROE (reported)	15.6	13.3	2.2	16.3	12.5	3.8	14.62	14.53	0.09

Source: Company data, Santander Brokerage Poland estimates

**Fig. 8. PKO – Forecast changes – Balance sheet**

PLN bn	2023E				2024E				2025E			
	New	Old	%	PLN bn	New	Old	%	PLN bn	New	Old	%	PLN bn
Total Assets	471.9	455.1	4	17	484.6	467.8	4	17	496.5	479.8	3	17
Bonds	168.8	152.0	11	17	176.1	158.9	11	17	182.7	165.2	11	17
Loans	241.8	242.6	0	-1	247.1	248.3	0	-1	252.5	254.1	-1	-2
Deposits	374.7	357.2	5	18	383.0	365.5	5	17	391.3	374.0	5	17
Equity	43.6	42.9	1	1	47.9	47.2	1	1	51.5	50.8	1	1
Mortgage loans	107.2	102.7	4	5	110.0	105.7	4	4	112.6	108.6	4	4
CHF mortgages	12.7	13.1	-3	0	10.3	10.7	-3	0	8.4	8.7	-3	0
Other retail loans	34.5	34.1	1	0	35.9	35.5	1	0	37.3	37.0	1	0
Corporate loans	104.2	110.3	-6	-6	106.3	112.5	-6	-6	108.4	114.7	-6	-6

Risk ratios (%)	New	Old	%	New	Old	%	New	Old	%
Cost of risk (%)	0.57	0.65	-0.09	0.63	0.64	-0.01	0.63	0.64	0.00

Capital & dividends	New	Old	%	New	Old	%	New	Old	%
Tier-1 (PLN bn)	44.1	42.5	1.6	47.2	45.1	2.1	50.9	45.1	5.8
Tier-2 (PLN bn)	2.7	2.7	0.0	2.7	2.7	0.0	2.7	2.7	0.0
TCR (PLN bn)	18.0	18.0	-0.1	18.4	18.5	-0.1	18.8	18.5	0.3
RWA (PLN mn)	207.8	208.5	-0.7	212.3	213.4	-1.1	216.9	213.4	3.5
CT1 ratio (%)	19.6	18.8	0.8	20.6	19.5	1.0	21.7	19.5	2.2
CAR ratio (%)	20.8	20.0	0.8	21.7	20.7	1.0	22.9	20.7	2.1
Div. payout (%)	50.0	50.0	0.0	50.0	50.0	0.0	50.0	50.0	0.0
Dividend (PLN mn)	0	1,625		3,072	2,611	462	3,720	2,611	1,109
No. of shares (mn)	1,250	1,250	0	1,250	1,250	0	1,250	1,250	0

Source: Company data, Santander Brokerage Poland estimates

# Santander Brokerage Poland

Jana Pawła II Avenue 17

00-854 Warszawa

fax. (+48) 22 586 81 09

## Equity Research

Kamil Stolarski, PhD, CFA, <i>Head of Equity Research Banks, Insurers, Strategy</i>	tel. (+48) 22 586 81 00	kamil.stolarski@santander.pl
Paweł Puchalski, CFA, <i>Equity Analyst Telecommunications, Metals &amp; Mining, Power</i>	tel. (+48) 22 586 80 95	pawel.puchalski@santander.pl
Tomasz Krukowski, CFA, <i>Equity Analyst Oil&amp;Gas, Pharma &amp; Biotech, CEE Non-Financials</i>	tel. (+48) 22 586 81 55	tomasz.krukowski@santander.pl
Adrian Kyrzcz, <i>Equity Analyst Construction, Real Estate, IT</i>	tel. (+48) 22 586 81 59	adrian.kyrzcz@santander.pl
Tomasz Sokołowski, <i>Equity Analyst Consumer, E-commerce</i>	tel. (+48) 22 586 82 36	tomasz.sokolowski@santander.pl
Michał Sopieli, <i>Equity Analyst Industrials, Chemicals, Quantitative Analysis</i>	tel. (+48) 22 586 82 33	michal.sopiel@santander.pl
Piotr Zielonka, CFA, <i>Equity Analyst Gaming, Strategy</i>	tel. (+48) 22 534 16 10	piotr.zielonka@santander.pl
Marcin Działek, <i>Analyst Technical Analysis</i>	tel. (+48) 22 782 93 09	marcin.dzialek@santander.pl

## Sales & Trading

<b>Kamil Kalemba, <i>Head of Institutional Equities</i></b>	tel. (+48) 22 586 80 84	kamil.kalemba@santander.pl
Mateusz Choromański, CFA, <i>Head of Sales Securities Broker, Investment Advisor</i>	tel. (+48) 22 586 80 82	mateusz.choromanski@santander.pl
Alex Kamiński	tel. (+48) 22 586 80 63	alex.kaminski@santander.pl
Błażej Leśków, <i>Securities Broker</i>	tel. (+48) 22 586 80 83	blazej.leskow@santander.pl
Michał Stępkowski, <i>Securities Broker</i>	tel. (+48) 22 586 85 15	michal.stepkowski@santander.pl
Marek Wardzyński, <i>Securities Broker</i>	tel. (+48) 22 586 80 87	marek.wardzynski@santander.pl
Adam Mizera, ACCA, CFA, <i>Securities Broker</i>	tel. (+48) 22 586 85 14	adam.mizera@santander.pl

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In preparing this report Santander Brokerage Poland applied at least one of the following valuation methods: discounted cash flows (DCF), comparative, mid-cycle, dividend discount model (DDM), residual income, warranted equity method (WEV), SOTP valuation, liquidation value.

**The discounted cash flows (DCF) valuation method** is based on expected future discounted cash flows. One advantage of the DCF valuation method is that it takes into account all cash streams reaching Issuer and the cost of money over time. Some disadvantages of the DCF valuation method are that a large number of parameters and assumptions need to be estimated; and the valuation is sensitive to changes in those parameters.

**The comparative valuation method** is based on the economic rule of "one price". Some advantages of the comparative valuation method are that the analyst need only estimate a small number of parameters; the valuation is based on current market conditions; the relatively large accessibility of indicators for companies being compared; and that there is an extensive knowledge of the comparative method among investors. Some disadvantages of valuation by the comparative method are the considerable sensitivity of the results of the valuation on the choice of companies to the comparative group; the method can lead to a simplification of the picture of the company which in turn can lead to omitting certain important factors (e.g. growth dynamics, extra-operational assets, corporate governance, the repeatability of results, differences in applied accounting standards); and the uncertainty of the effectiveness of a market valuation of companies being compared.

**The mid-cycle multiple valuation** is based on long-term average valuation multiples of a sector or a peer group. The methodology aims to calculate a fair, through the cycle value of the company. Among its shortfalls is that at peaks and/or troughs of the cycle, the implied fair value may deviate substantially from the market's value of an analysed stock as well as the methods' reliance on the quality of external data (we usually use Bloomberg or Damodaran databases). Simplicity and average through-cycle value allowing to capture over- as well as under-valuation of a given stock are the main advantages of this methodology.

**The dividend discount model (DDM) valuation** is based on the net present value of the future dividends that are expected to be paid out by the company. Some advantages of the DDM valuation method are that it takes into account real cash flows to equity-owners and that the methodology is used in respect to companies with long dividend payout history. Main disadvantage of the DDM valuation method is that dividend payouts are based on a large number of parameters and assumptions, including dividend payout ratio.

**Residual income method** is conceptually close to the discounted cash flows method (DCF) for non-financial stocks, the difference being that it is based on expected residual income (returns over COE) rather than expected future cash flows. One advantage of this valuation method is that it captures the excess of profit potentially available to shareholders and the cost of money over time. Main disadvantage of the valuation method is that a large number of parameters and assumptions need to be estimated; and the valuation is sensitive to changes in those parameters.

**The warranted equity method (WEV)** is based on the formula  $P/BV = (\text{two year forward ROE less sustainable growth rate}) / (\text{Cost of equity less sustainable growth rate})$  which allows estimating a fair value (FV) of a given stock in two years' time. Subsequently the FV is discounted back to today. The main advantage of the WEV method is that it is a transparent one and based on relatively short term forecasts, hence substantially reducing the margin of forecasting error. The main disadvantage in our view is that the model is based on the principle that stock price should converge towards its fair value implied by company's ROE and COE.

**SOTP valuation** - different assets of a company are being valued according to different valuation methods, and the sum of these valuations represents the final valuation of the company. SOTP valuation advantages / disadvantages are identical to advantages and disadvantages of the specific valuation methods used.

**Liquidation value method** - liquidation value is the estimated amount of money that an asset or company could be quickly sold for, such as if it were to go out of business. Then, the estimated assets value is adjusted for liabilities and liquidation expenses. One advantage of this valuation method is its simplicity. This method does not account for intangible assets as goodwill, which is the main disadvantage.

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