Polish Banks: Consolidation into Domestic Ownership Should Continue

The Polish banking sector appears as one of the most dynamic in the CEE region. Historically characterised by strong foreign ownership, domestic players have recently initiated a trend towards consolidation and 'nationalisation', by acquiring controlling stakes in banks which were previously foreign-owned. Although this has mainly been driven by financial viability considerations, political pressure has also played an important role.

In this brief report, Scope aims to provide an overview of some of the most recent M&A transactions, including the acquisition of Bank Pekao, and outline how these have changed the competitive banking landscape in Poland. We also look at potential further developments, and try to estimate their impact on the sector's structure.

At this time Scope does not have public ratings on Polish banks.

According to data from the Polish financial supervision authority, KNF, and the National Bank of Poland, subsidiaries of Western institutions have historically made up the majority of banks in the country, measured in terms of total balance sheet size.

In recent years this proportion has been declining steadily: we estimate that as of H1 2017 this trend has finally reversed, with the share of total assets held by domestic banks (either private, public or cooperative) standing at approx. 53%.

Figure 1: Breakdown of banking assets by ownership structure 2011-1H2017E

	2011	2012	2013	2014	2015	2016E	1H17E
Publicly-controlled banks	22.2%	23.0%	22.3%	24.1%	23.9%	27.5%	36.9%
Private banks	67.4%	66.4%	66.2%	64.9%	65.3%	61.7%	51.0%
o/w domestic private banks	4.6%	5.0%	5.3%	5.5%	8.3%	4.7%	4.6%
o/w foreign-owned banks	62.8%	61.4%	60.9%	59.4%	57.0%	57.0%	46.4%

Source: NBP, KNF, Scope Ratings
Banks under public control: BGK, Bank Pocztowy, PKO BP, PKO Bank Hipoteczny, BOŚ Bank, Alior from 2016 and Pekao in H1 2017, excludes cooperative and other banks

In the last few years, the following transactions have played a role in this process:

1) In 2014, PKO Bank Polski (PKO), which is controlled by the state treasury, bought the banking and insurance operations of Nordea Group in Poland (Nordea Bank Polska) and, in 2016, the leasing operations of Raiffeisen Bank Polski.

   Through these acquisitions, PKO, the largest Polish bank in terms of assets, grew its balance sheet by almost 50% between 2012 and H1 2017. PKO is a market leader in the traditional mortgage lending business, where, together with PKO Mortgage Bank, it commands more than a quarter of the market. It is also a major player in the retail lending business with a market share of approx. 23%. The acquisition of RB Polski's leasing business also allowed PKO to double its presence in the factoring business, obtaining a 13.30% market share at YE 2016.

2) In 2015 the state insurance company PZU bought Alior. In turn, Alior acquired the core activities of Bank BPH, the Polish unit of General Electric Capital, in 2016.

3) In 2017 UniCredit sold a 32.8% stake in Pekao to PZU and the Polish Development Fund (PFR).

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We estimate that by acquiring controlling stakes in Alior and, with PFR, in Pekao, PZU has gained relevant influence on more than 15% of total commercial banking assets (excluding cooperative banks) as of H1 2017.

Alior and Pekao: plausible alliance

Alior is the ninth-largest commercial bank, with PLN 61.8bn in assets as of H1 2017. Predominantly a retail and micro/SMEs bank, Alior's model differs from that of traditional banks due to a strong digital proposition combined with a comparatively large physical network, which the bank plans to scale back by 2020. Alior is still managing the effects of the Bank BPH acquisition: the integration process between Alior and the core activities of Bank BPH will not be complete until 2019, and has so far produced costs but not synergies, which are expected to arise between 2017 and 2019. In contrast to Alior, Pekao's business model is clearly corporate-oriented, with the bank playing a leading role in project and leveraged finance as well as debt capital markets.

Given the significant divergence between the two banks' business models, there is no immediately discernible benefit to be gained from merging the two entities: as Pekao's management team noted, the two banks' offerings might be additive but a merger would entail low cost synergies. We believe, given the fact that Pekao has fallen somewhat behind in terms of innovation and in catching the digital wave, the two banks might consider agreements on technology transfers. This possibility has been confirmed by the acting management team, which mentioned that deals on the procurement side might be an option in Pekao's near future, with the aim of reducing the cost base. Moreover, the merger is likely be opposed by the KNF as it would curtail competition in the market.

Of the top five commercial banks, Zachodni, mBank and ING Bank Slaski together represent the remaining 21% of assets. These banks are subsidiaries of large west European banks: Santander, Commerzbank and ING, respectively.

Figure 2: Market shares of the top five commercial banks by assets

Market shares	Retail mortgage loans	Retail loans	Corporate loans	Retail deposits	Corporate deposits	Leasing	Factoring	Mutual funds
PKO Bank Polski	25.7%	22.8%	na	20.7%	na	13.3%	6.2%	7.6%
Pekao	18.0%	8.9%*	14%*	9.9%*	14%*	na	8.7%	16.9%
Bank Zachodni	14.3%	na	na	10.3%		7.0%	12.0%	na
mBank	7.5%	6.5%	6.1%	6.1%	10.1%	6.9%	7.3%	na
ING Bank Śląski	5.3%	5.0%	10.5%	8.9%	8.0%	na	15.4%	na

Source: Company data, Scope Ratings Note: *for Pekao figures as of Q1 2016, factoring turnover as of YE2016 (PFA)

Plans for Raiffeisen Bank Polska IPO on hold

Raiffeisen Bank Polska is the subsidiary of Raiffeisen Bank International (RBI) in Poland and the 10th largest bank in terms of assets. We estimate its market share at around 3.3% for both retail and corporate lending.

In July, RBI decided to suspend the IPO process for its Polish subsidiary. The KNF requested RBI to float a minimum of 15% of shares on the Warsaw Stock Exchange, as a condition for the acquisition of Polbank by RBI's Polish unit in 2012. The deadline, originally set for H1 2016, was postponed by one year and is now set for May 2018. In the meantime, discussions regarding a potential acquisition by Alior have ended.

Even though the timeline for a potential IPO is now in doubt, RBI is still planning to go ahead with the listing. A minority listing would be the preferred option for the bank to boost its capital ratios.

Although an acquisition agreement cannot be excluded, RB Polska would have to keep its sizeable foreign-exchange mortgage portfolio, as the regulator demands that foreign lenders retain foreign-exchange-denominated mortgages when exiting the Polish market.

More M&A to come

Another potential target for acquisition is Deutsche Bank Polska, with PLN 40bn in assets as of YE2016. We would see as plausible an acquisition by a state-controlled player as well as a foreign-owned bank: Millennium BCP, which controls the polish Bank Millennium, and Bank Zachodni are interested in the deal. This would confirm the consolidation trend in the sector.

Recent experience shows how high banking taxes and contributions, tight supervision and fierce competition are challenging smaller players in the sector. These considerations are outweighing the benefits deriving from strong economic growth, which often lead to double-digit ROEs when a critical mass is reached

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