

Banque Pour Le Commerce Exterieur Lao

TP kip 10,500;
US\$ 1.31

The largest bank with the highest growth in Laos

Key highlights

The largest bank with greatest banking network in Laos

BCEL is the largest state-owned bank with the biggest market share (with asset size of US\$1500mn or representing 40% of bank sector assets) and provides a full range of financial products and services. Due to its largest exposure on corporate & SME loans, most extensive processing network for the business sector, and strong relationships with more than 100 banks internationally, BCEL is well-positioned to benefit under rapid economic growth.

High growth potential bank

Being a state-owned bank enables BCEL to gain better business opportunities, lending growth potential, and creditworthiness among local and international counter parties. With its superior profile, we believe 3-yr CAGR loan growth of 30% (with margin of 2.4%) and non-interest income growth of 25% is sustainable over the next three years. Note that interest income represents 35% of total revenue while non-NII is 65%.

Gaining benefit on interest rate/exchange rate parity

The majority of its deposits (58% of BCEL's total deposits) are still foreign currencies with a relatively low rate of 1-1.5%, while the lending rate has been relatively high. This enables BCEL to earn a high loan spread at 8-9% as well as substantial forex income.

Fair price 10,500 kip or 1.31 USD (PBV 1.45x)

As Lao accounting standards on NPL classification and provision policies are more relaxed than international peers, we adjust the additional loan reserve into its book value. Target PBV under the Gordon growth model (ROE-g/COE-f) suggests BCEL's fair PBV at 1.45x, implying a fair price at 10,500 kip or 1.31 USD.

Financial and Valuation

| FY Ended 31 Dec | 2009 | 2010 | 2011E | 2012E | 2013E |
|--------------------|------|------|-------|-------|-------|
| PPOP (USD mn) | 16.7 | 22.7 | 36.6 | 48.3 | 65.6 |
| Provision (USD mn) | -0.8 | -2.4 | -5.1 | -6.8 | -9.2 |
| NP (USD mn) | 10.5 | 13.6 | 24.3 | 29.0 | 39.5 |
| EPS (USD) | 0.08 | 0.10 | 0.18 | 0.21 | 0.29 |
| EPS growth (%) | n.a. | 22% | 89% | 23% | 30% |
| Book value (USD) | 0.36 | 0.71 | 0.91 | 1.06 | 1.32 |
| Dividend USD) | n.a. | n.a. | 0.09 | 0.06 | 0.09 |

| FY Ended 31 Dec | 2009 | 2010 | 2011E | 2012E | 2013E |
|-----------------|-------|-------|-------|-------|-------|
| PER (X) | 12.2 | 10.0 | 5.3 | 4.4 | 3.2 |
| PBV (X) | 2.61 | 1.39 | 1.03 | 0.89 | 0.71 |
| Div. yield | n.a. | n.a. | 10.2% | 7.3% | 10.0% |
| ROE (%) | 21.4% | 13.9% | 19.5% | 20.1% | 21.9% |

Share data

| | |
|--------------------------|-----------------|
| LSX code/ Bloomberg | BCEL.LS/BCEL LS |
| Sector | Bank |
| Price (Kip/USD) | 7,500/0.95 |
| Paid-up Shares (m sh) | 136.6 |
| Market cap (USD mn) | 119.4 |
| 52 week High / Low (USD) | 1.88/0.86 |
| Avg. daily T/O (shares) | 90,890 |
| Company Website | www.bcel.com.la |

Stock Performance (%)

| | 1M | 3M | YTD |
|----------|------|------|------|
| Absolute | -13% | -23% | -14% |



Company Profile

Banque pour le Commerce Exterieur du Lao accepts deposits and offers commercial banking services. The bank offers personal and business loans, bank guarantees, internal and international payments, and credit cards.

Note:

BCEL-KT Securities Co.,ltd is a joint venture company between BCEL bank and KTZMICO Securities (Thailand)

This paper is a co-operation between
the BCEL-KT and KTZMICO teams
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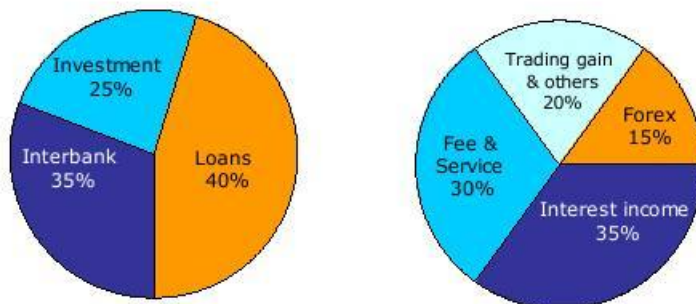
Company background

Banque Pour Le Commerce Exterieur Lao (BCEL) was established in 1975 and became a full commercial bank in 1986. It provides a full range of financial services including lending (mainly to wholesale banking in corporate loans & SME loans), the insurance business, settlement banking, forex dealing and financial investment. At present, the bank has 18 branches and 22 service units nationwide. The bank has established business relations with more than 100 banks internationally, allowing it to hold the largest share of cross-border money transfer services and have the largest processing/settlement network for the business sector and importers/exporters.

Largest bank with 40% market share

The value of the bank's total assets as of Jun-11 was 12,266,505 million kip (about US\$1,531 million), representing a 40% market share of the total financial industry in Laos. In terms of income breakdown, around 35% comes from interest on loans, 35% percent from service fees and ATM fees, 10% percent from exchange rate services, and 20% from trading income on precious metals and investments.

Figure 1: Earnings assets and income breakdown



Source: BCEL, KT ZMICO Research

Figure 2: BCEL's business group structure

| | Operation start | BV (Kip Bn) | Industry | % ownership |
|----------------------------------|-----------------|--------------|-------------------|-------------|
| BCEL Leasing Ltd | 2009 | 9.0 | Banking & Finance | 100% |
| BCEL - Krung Thai Securities Ltd | 2010 | 21.0 | Securities | 70% |
| Lao Viet Joint Venture Bank | 2000 | 63.53 | Banking & Finance | 50% |
| Banque Franco - Lao Ltd | 2009 | 138.0 | Banking & Finance | 46% |
| Lao-Viet Insurance Joint JV | 2008 | 7.37 | Insurance | 29% |
| Total | | 239.1 | | |

Source: BCEL, KT ZMICO Research

Became listed company in the Lao Stock Exchange at end of 2010

BCEL became a listed company in November 2010 after distributing 27.32 million shares or 20% of total shares to the public. On top of the IPO shares, 75% of total shares were allotted to Lao citizens and 25% to BCEL's staff. Recently, as part of the privatization plan, the government signed an MOU to sell 10% of total shares to a foreign strategic partner, the Cofibred, a subsidiary of France's second largest bank.



High growth profile bank

Stronger economic momentum to benefit the bank

One of the main impetuses to support the bank's long-term prospects is the expectation of stronger economic momentum in the coming years. As mentioned in the macroeconomic section, the Lao PDR is in the midst of a major transformation. This shift from a purely agricultural economy into a more industrialized economy has helped boost economic growth toward 8% YoY over the past years. The stronger economic growth profile will translate into more demand for loans in the coming periods. Furthermore, the country's integration into the wider regional economy and its emergence as a key transportation corridor and power generation hub will allow it exploit its rich natural resources, which means more businesses will open. Finally, there is a strong likelihood that the country will eventually become a WTO member (it is now in the final round of negotiations), with this further enhancing the prospects for its businesses.

BCEL is well placed to benefit from rapid economic expansion

In the fast growing economy, BCEL is well placed to benefit given its strong banking presence and largest banking channel and processing network in Laos. In addition, being the largest state-owned bank enables it to raise deposits at a very low cost and gain substantial business loan volume. This in turn allows it to earn several kinds of fees from the business sector and intra-Indo China trade.

More room to improve the level of access to financial services

The Lao PDR's financial sector is still at an early stage, with some constraints in terms of access to financial services. Only 30-35% of Lao citizens are able to access financial services according to ADB research in 2009. In addition to the lack of a borrower's assessment system, credit extension is mainly made to licensed businesses or government-related projects. These factors offer plenty of room for financial sector improvement.



Enjoying high loan yield and spread

As around 55-60% of deposits are in foreign currency CASA (with the rate standing very low at 1-1.5%) and lend in relatively high rate on both local Kip and foreign currency, BCEL enjoys a high loan margin (at 8-9%) on the wide interest rate gap between the two currencies. As this interest rate/exchange rate parity has remained unchanged for some time, the relatively high loan spread should be sustained over the next 2-3 years.

% Deposits breakdown by currency (converted into LAK)

| Unit: LAK bn | 2010 | By percent |
|------------------------------|----------------|-------------|
| Deposits in LAK | 3,268.7 | 42% |
| Deposits in foreign currency | 4,429.2 | 58% |
| Total | 7,697.8 | 100% |

Source: BCEL's audited financial statement

Type of deposits

| Unit: LAK bn | 2010 | By percent |
|----------------------------|--------------|-------------|
| Current and savings (CASA) | 5,700 | 73% |
| Fixed term deposits | 1,944 | 25% |
| Margin deposits and others | 195 | 2% |
| Total | 7,839 | 100% |

Source: BCEL's financial note

Deposit rates in LAK and USD currency

| | Savings rate | Fixed rate (3M/12M) |
|-----|--------------|------------------------|
| USD | 1-1.5% | 1.75% / 3.0% |
| LAK | 3.50% | 6% / 10% |

Source: BCEL, BoL

% Loans breakdown by currency (converted into LAK)

| Unit: LAK bn | 2010 | By percent |
|--------------|----------------|-------------|
| Loans in LAK | 1,024.6 | 37% |
| Loans in USD | 1,371.2 | 50% |
| Loans in THB | 341.8 | 13% |
| Total | 2,737.6 | 100% |

Source: BCEL's audited financial statement

Lending rate by currency

| | O/D | S-T to L-T |
|---------------|-----|--------------|
| - USD and THB | 10% | 7.75 - 8.25% |
| - LAK | 14% | 9.0 - 13.0% |

Source: BCEL, BoL



Earnings performance and key assumptions

Non-NII is main earnings driver at 65-70% of revenue

As a result of the rapid economic changes, BCEL's earnings growth has come on very strong during the past three years with CAGR of 26%. Beyond that, Non-NII is the major earnings driver as it accounts for 65-70% of revenue with 3-yr CAGR of 56%. For 2011-2013, we assume growth at 25%.

NII represents 35% of revenue

Loans are not the major active asset in BCEL's balance sheet as they represent only 30% of total assets. Rather, investment in government securities and money market lending are the key assets. Given the asset mix being unchanged, forward NIM should remain on track with the historical range of 2.2-2.8%. We assume NIM of 2.4% over the next three years.

Provisioning policy and opex should move upward

The attempt to adopt the international financial framework will result in a gradual change in BCEL's accounting practices, including its provisioning policy, NPL reclassification, and operating expenses. To comply with international standards, NPLs should double and the provisioning expense-to-loan ratio should be 1% of loans (vs. 0.35% at the current), while operating expense growth should move upward (at +20% over the next three years).

Figure 3: BCEL's earnings assumptions and key figures

| Unit: USD mn | 2009 | 2010 | 6M11 | 2011E | 2012E |
|--|--------------|--------------|--------------|--------------|--------------|
| NII | 10.44 | 15.38 | 9.47 | 22.94 | 29.73 |
| Non-NII | | | | | |
| - Fees | 9.47 | 12.28 | 8.09 | 18.58 | 23.15 |
| - Forex | 4.33 | 5.18 | 4.63 | 8.11 | 10.14 |
| - Trading income & other | 8.63 | 10.97 | 8.24 | 15.94 | 19.18 |
| Total revenue | 32.9 | 43.9 | 30.4 | 65.6 | 82.2 |
| PPOP | 17 | 21 | 20 | 35.2 | 45.4 |
| LLP | (0.84) | (2.24) | (0.22) | (4.76) | (6.43) |
| Income tax | (5.41) | (6.37) | (0.92) | (7.61) | (11.71) |
| Net profit | 10.47 | 13.58 | 19.47 | 24.20 | 28.92 |
| Key figure and ratio | | | | | |
| NII: Non-NII | 32:68 | 35:65 | 32:70 | 35:65 | 36:64 |
| Loan growth | 138% | 42.2% | 33%* | 50% | 35% |
| Deposit growth | 29% | 41% | 20%* | 60% | 35% |
| Loan / deposit ratio | 38% | 38% | 41% | 43% | 45% |
| Average yield | 4.0% | 4.5% | 4.1% | 4.9% | 4.7% |
| Cost of fund | 1.58% | 1.72% | 1.89% | 2.22% | 2.34% |
| Net interest margin | 2.4% | 2.8% | 2.16% | 2.40% | 2.40% |
| Non-NII/gross rev | 68% | 65% | 69% | 63% | 63% |
| Cost to income ratio | 58% | 58% | 40% | 51% | 47% |
| NPLs | 1.74 | 8.49 | n.a. | n.a | n.a |
| % NPL/loans | 0.7% | 2.5% | n.a. | n.a | n.a |
| NPL coverage | 364% | 64% | n.a. | n.a | n.a |
| Credit cost (Provision expenses/loans) | 0.38% | 0.71% | 0.05% | n.a | n.a |

Source: BCEL, KT ZMICO Research

*YTD growth



Valuation – fair price 10,500 kip or 1.31 USD (PBV 1.45x)

Very strong growth in 1H11 earnings due to exceptional items

BCEL reported 1H11 earnings at 157,577 billion kip or 19.5 million USD, +70% YoY as a result of lower LLP and almost zero income tax (vs. 30% for normal rate). Excluding these items, PPOP growth should be -4% YoY. The key drags were lower NII (as a result of low NIM at 1.8% vs. 2.2-2.8% for the normal range) and softer non-NII growth (+7% YoY).

More relaxed accounting standards than international peers have caused BCEL’s key profitability indicators (ROA, ROE) and asset quality to be overstated. The current NPL ratio of 2.5% should be revised up, while the loan loss reserve should be increased twofold. Putting these numbers into our calculation, BCEL’s tangible book value at year end 2011F should be 7242 kip (-6% from stated-BV). With L-T ROE of 18%, BCEL deserves PBV at 1.45x (as shown in the table below), which implies value of 10,500 kip.

Figure 4: Valuation calculation

| | |
|--|-----------------------------------|
| Target PBV using Gordon model (ROE-g)/CoE-g | |
| Dividend payout ratio | 30% |
| Long-term ROE | 18% |
| Cost of equity (COE) (CAPM) | 16% |
| where | g = (Avg. 5yr-ROE*Retention rate) |
| | beta = 1 |
| | risk free = 6% |
| | risk premium = 10% |
| Target P/BV = (ROE-g)/(CoE-g) | 1.45 |
| Book value at year end-2011F (kip) | 7,242 |
| BCEL’s fair price (kip) | 10,500 |
| BCEL’s fair price (in USD) | 1.31 |

Source: BCEL, KT ZMICO Research



Key concerns

Difference in accounting policies

Under Lao regulations, loans at banks are classified into six grades (as described in the table below). Although NPLs are defined as loans overdue >90 days (same as the international standard), provision expenses on each asset class are still widely different. Loans overdue 90-180 days require a specific provision at just 20% vs. 100% for the international standard.

Figure 5: Loan classification and provisioning policy differ

| Loan grade | Loan classification | Days delinquent | Loan status | | Specific provision rate | |
|------------|---------------------|-----------------|----------------|----------------|-------------------------|---------------|
| | | | Laos | International | Laos | International |
| A,B | Current | <90 days | Performing | Performing | 0% | 1% |
| C1 | Special mention | <90 days | Performing | Performing | 0% | 2% |
| C2 | Substandard | 91-180 days | Non-performing | Non-performing | 20% | 100% |
| D | Doubtful | 181-360 days | Non-performing | Non-performing | 50% | 100% |
| E | Loss (NPL) | >360 days | Non-performing | Non-performing | 100% | 100% |

Source: BCEL's financial statement, KT ZMICO Research

Capital adequacy ratio (CAR)

| | By value (kip mn) | By value (USD mn) |
|--|-------------------|-------------------|
| Tier I | 887,390 | 111 |
| Tier II | 14,362 | 1.79 |
| Total | 901,752 | 112.58 |
| Less: Investments in other credit and financial institutions | 232,826 | 29.07 |
| Total Capital | 668,926 | 83.51 |
| Risk weighted assets (RWA) | 4,959,049 | 619.11 |
| CAR | 13.49% | 13.49% |

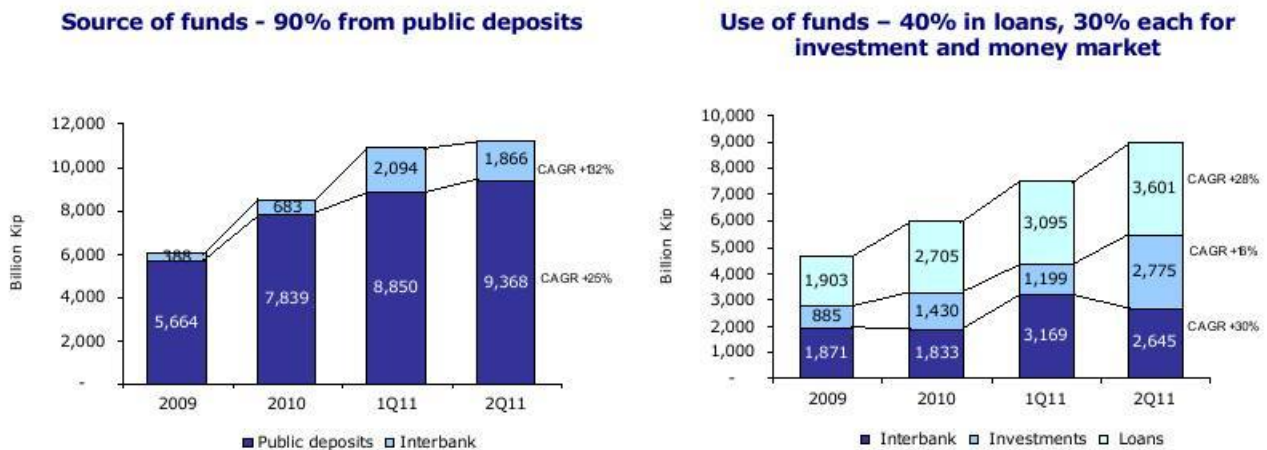


Appendix

Source of funds – around 90% comes from public deposits

By being a state-owned bank with the largest processing network for the business sector, BCEL has been able to gain a greater deposit base from the retail and local business sector than other state-owned banks. Its deposit base has grown consistently at 25%, with stable costs of around 1.8-1.9% over the past five years.

Figure 6: BCEL’s source of funds vs. use of funds (kip bn)



Source: BCEL, KT ZMICO Research

Figure 7: BCEL’s loan breakdown



Source: BCEL's financial data, KT ZMICO Research

Figure 8: BCEL’s non-performing loans and provision coverage ratio

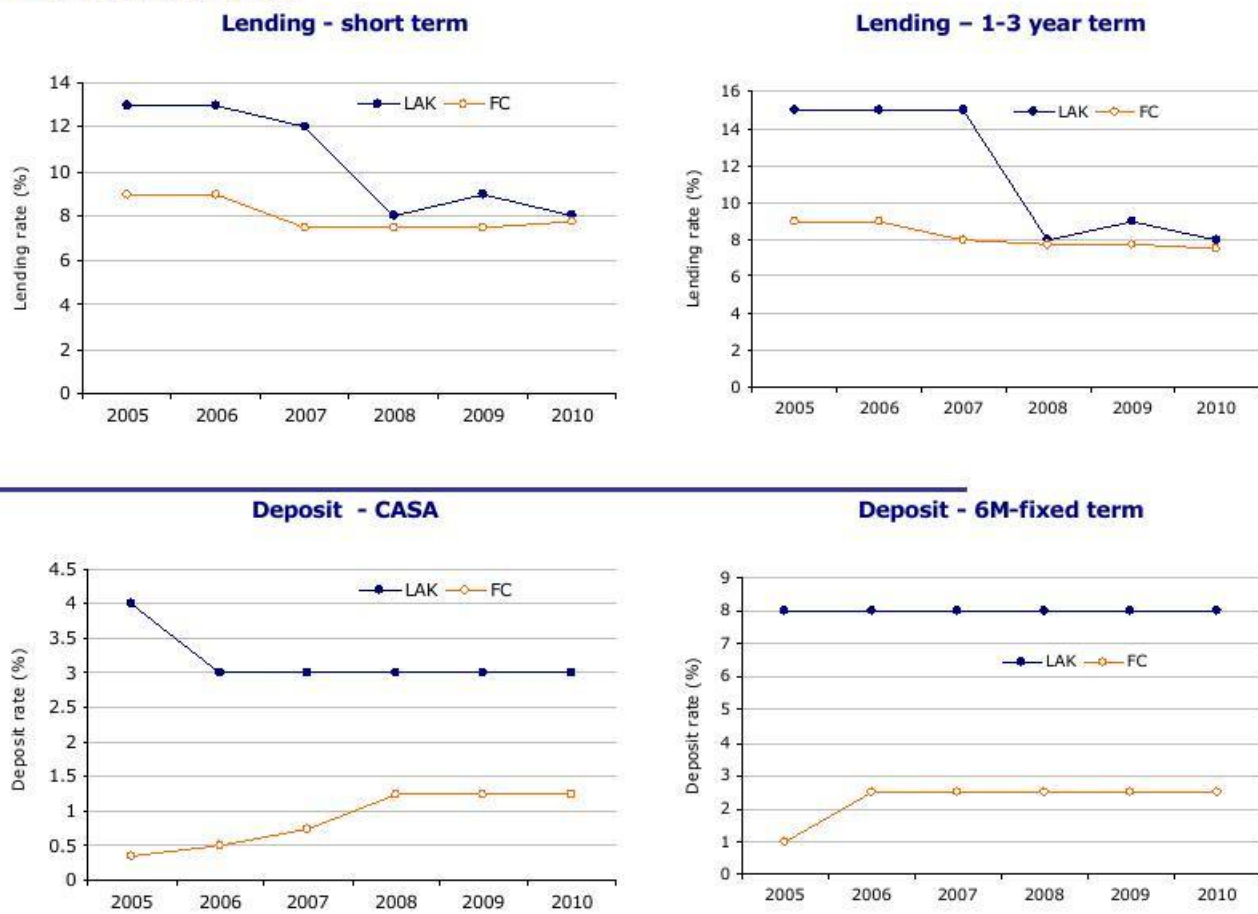
| Unit: LAK bn | 2008 | 2009 | 2010 |
|-----------------------------|--------------|--------------|--------------|
| Performing loans | 1,380 | 1,902 | 2,669 |
| Non-performing loans (NPLs) | 21 | 14 | 68 |
| Total loans | 1,400 | 1,916 | 2,738 |
| % NPL ratio | 1.5% | 0.7% | 2.5% |
| % LLR/loans (NPL coverage) | | 364% | 87% |

Source: BCEL, KT ZMICO Research

Historical interest rates

As a result of the country being in the early stages of financial development and the low level of access to financial services, the interest rate trend has been somewhat distorted, i.e., the interest rate direction (both the deposit rate and lending rate) in Laos has not correlated to the loanable demand framework and has not corresponded to the global interest rate trend. Deposit rates for both CASA and fixed term deposits have been relatively flat for the past five years, while the lending rate has been on the decline. Thus, interest rates seem to be determined by the stability of the local kip currency and foreign currency.

Figure 9: Historical rates



Source: Company data, KT ZMICO Research

Figure 10: BCEL's financial table

| | 2009 | 2010 | 6M11 | 2011F | 2012F | 2013F |
|--|-------------|-------------|-------------|-------------|-------------|--------------|
| Exchange rate (Kip/USD) | 8,522 | 8,041 | 8,010 | 8,010 | 8,010 | 8,010 |
| (Unit: USD mn) | | | | | | |
| Interest income | 21.6 | 33.7 | 22.8 | 57.0 | 75.7 | 103.2 |
| Interest expense | (11.2) | (18.3) | (13.4) | (34.0) | (46.0) | (62.1) |
| Net interest income | 10.4 | 15.4 | 9.5 | 22.9 | 29.7 | 41.1 |
| Fee & service income | 9.5 | 12.3 | 8.1 | 18.6 | 23.2 | 28.5 |
| Total non-interest income | 17.4 | 21.2 | 16.9 | 33.9 | 42.0 | 51.7 |
| Operating income | 32.9 | 43.8 | 30.4 | 65.6 | 82.2 | 105.3 |
| Operating expenses | (16.1) | (21.1) | (10.5) | (29.0) | (33.9) | (39.7) |
| Operating profit before provision | 16.7 | 22.7 | 20.0 | 36.6 | 48.3 | 65.6 |
| Provisioning charges | (0.8) | (2.4) | 0.6 | (4.2) | (6.8) | (9.2) |
| Operating profit after provision | 15.9 | 20.3 | 20.6 | 32.4 | 41.5 | 56.4 |
| Exceptional items | - | - | - | - | - | - |
| Profit before income tax | 15.9 | 20.3 | 20.6 | 32.4 | 41.5 | 56.4 |
| Income tax | (5.4) | (6.7) | (1.0) | (8.1) | (12.4) | (16.9) |
| Minority interest | - | - | (0.1) | - | - | - |
| Net profit | 10.5 | 13.6 | 19.6 | 24.3 | 29.0 | 39.5 |
| Reported EPS | 0.08 | 0.10 | 0.14 | 0.18 | 0.21 | 0.29 |
| Fully diluted EPS | 0.08 | 0.10 | 0.14 | 0.18 | 0.21 | 0.29 |

Source: KT Zmico estimates

Figure: Key Ratios

| | | | | | | |
|-------------------------------|-------|-------|-------|-------|-------|-------|
| Revenue Growth (%) | n.a. | 26% | -17% | 49% | 25% | 28% |
| PPOP Growth (%) | n.a. | 28% | -4% | 61% | 32% | 36% |
| EPS Growth (%) | n.a. | 22% | 70% | 78% | 19% | 36% |
| Net Loan growth (%) | n.a. | 42% | n.a. | 50% | 35% | 35% |
| Provision charge to loans (%) | 0.38% | 0.70% | 0.07% | 0.83% | 1.00% | 1.00% |
| Yield on Avg Assets (%) | 4.0% | 4.5% | 4.1% | 4.9% | 4.7% | 4.9% |
| Cost of Funds (%) | 1.6% | 1.7% | 1.9% | 2.4% | 2.3% | 2.6% |
| NIM (%) | 2.4% | 2.8% | 2.2% | 2.4% | 2.4% | 2.4% |
| Cost to income ratio (%) | 49% | 48% | 34% | 44% | 41% | 38% |
| Effective tax rate (%) | 34% | 33% | 5% | 25% | 30% | 30% |

Source: KT Zmico estimates

Figure : Consolidated Balance Sheet

(Unit: Btm)

| | | | | | | |
|---|--------------|----------------|----------------|----------------|----------------|----------------|
| Interbank & securities under resale | | | | | | |
| Investment in securities | 103.9 | 177.8 | 346.5 | 223.1 | 256.6 | 230.9 |
| Loans & accrued interest receivable-net | 223.3 | 336.5 | 449.6 | 506.6 | 684.0 | 923.4 |
| Other assets | 224.3 | 449.0 | 405.0 | 521.9 | 542.9 | 550.0 |
| Total assets | 771.0 | 1,191.2 | 1,531.4 | 1,695.9 | 2,149.2 | 2,636.3 |
| Deposits | 664.6 | 974.8 | 1,169.6 | 1,321.1 | 1,684.4 | 2,041.5 |
| Borrowings | - | - | - | - | - | 0.0 |
| Total liabilities | 722.0 | 1,093.6 | 1,417.0 | 1,571.7 | 2,004.9 | 2,456.1 |
| Minority interests | - | - | - | - | - | 0.0 |
| Shareholders equity | 49.1 | 97.6 | 113.2 | 124.3 | 144.4 | 180.2 |
| Total Liab.&Shareholders' equity | 771.0 | 1,191.2 | 1,531.4 | 1,695.9 | 2,149.2 | 2,636.3 |

Source: KT Zmico estimates

Source: BCEL's financial data, KT ZMICO Research



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