

Adjusting PO for higher costs



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A high loan/deposit ratio may limit cost cuts

Garanti is the only Turkish bank under our coverage that has reached 100% loan to deposit ratio. So far, the bank has managed to outpace competition in growth in both placements and funding and we still expect it to be an outlier going into 2008. However, taking into consideration that it may shy away from international borrowing, we are increasing our deposit cost assumptions for the bank. The result is a lower NIM of 5.2% - a 40bps decline from earlier expectations. We are also lowering our bottom line forecast by an average of 3% for the 2007-2009 period.

New PO at TRY12.1 - a 2% downward adjustment

The changes to our forecasts lead to a minor adjustment our PO. The stock is now trading at 8x 2009E P/E and 1.7x P/B. We maintain our Buy call with 38% upside.

How much should we read into GE's stake sale?

GE sold 5% stake in Garanti at 25% discount to mcap. Both major shareholders' comments are for continuing cooperation but we are now questioning if this may be interpreted as diminishing interest of GE in Turkey. And if so, would this affect Garanti's appetite for Halkbank privatisation?

Estimates (Dec)

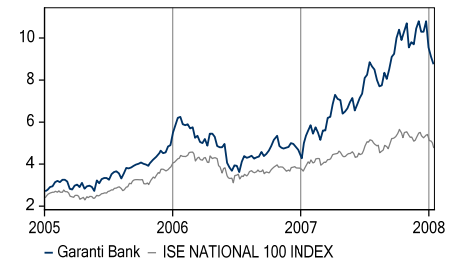
(TRY)	2005A		2006A		2007E		2008E		2009E	
	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP	
Net Profit	672	978	2,186	1,953	2,295					
EPS (Reported)	0.32	0.47	1.04	0.93	1.09					
EPS - fully diluted	0.32	0.47	1.04	0.93	1.09					
Dividend / Share	0.05	0.05	0.11	0.15	0.18					
Adjusted NAV PS	1.80	2.20	3.26	4.04	4.98					
BVPS	1.83	2.22	3.28	4.06	5.00					

Valuation (Dec)

	2005A	2006A	2007E	2008E	2009E
Price / Earnings	27.2x	18.7x	8.4x	9.4x	8.0x
EPS Change (YoY)	49.2%	45.5%	124%	-10.7%	17.5%
Price / BV	4.76x	3.91x	2.65x	2.14x	1.74x
Price / NAV	4.82x	3.95x	2.67x	2.15x	1.75x
Net Yield	0.57%	0.57%	1.30%	1.74%	2.04%
DPS Change (YoY)	NA	0%	127%	33.3%	17.5%
Price / GOP	13.1x	11.4x	5.88x	5.94x	4.97x

Stock Data

Price	TRY8.70
Price Objective	TRY12.40 to TRY12.10
Date Established	21-Jan-2008
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	TRY4.85-TRY11.20
Mrkt Val / Shares Out (mn)	TRY18,270 / 2,100.0
Average Daily Volume	16,610,792
ML Symbol / Exchange	TKGBF / IST
Bloomberg / Reuters	GARAN TI / GARAN.IS
ROE (2007E)	37.8%
Total Dbt to Cap (Dec-2006A)	0%
Est. 5-Yr EPS / DPS Growth	29.4% / 48.7%
Free Float	52.0%



21 January 2008

iQprofileSM Garanti Bank

Key Income Statement Data (Dec)	2005A	2006A	2007E	2008E	2009E
(TRY Millions)	Other GAAP	Other GAAP	Other GAAP	Other GAAP	Other GAAP
Net Interest Income	1,675	1,902	2,605	3,426	3,921
Net Fee Income	738	1,014	1,286	1,628	1,980
Securities Gains / (Losses)	116	(56.3)	0	0	0
Other Income	174	213	1,001	164	168
Total Non-Interest Income	1,028	1,171	2,287	1,791	2,148
Total Operating Income	2,702	3,073	4,892	5,217	6,069
Operating Expenses	(1,308)	(1,465)	(1,785)	(2,141)	(2,390)
Pre-Provision Profit	1,394	1,608	3,106	3,077	3,679
Provisions Expense	(447)	(325)	(318)	(487)	(628)
Operating Profit	947	1,283	2,788	2,590	3,051
Non-Operating Items	3.14	46.9	49.4	52.1	54.2
Pre-Tax Income	951	1,330	2,838	2,642	3,105
Net Income to sh/holders	672	978	2,186	1,953	2,295
Adjusted Cash Earnings	672	978	2,186	1,953	2,295

Key Balance Sheet Data

Total Assets	36,425	50,287	61,902	74,247	88,674
Average Interest Earning Assets	28,174	40,818	53,623	65,412	78,631
Weighted Risk Assets	20,394	27,377	38,390	49,171	62,154
Total Gross Customer Loans	17,633	27,801	37,533	49,474	63,896
Total Customer Deposits	22,833	30,139	36,332	44,326	53,191
Tier 1 Capital	3,294	4,473	6,301	7,944	9,923
Tangible Equity	3,841	4,670	6,888	8,531	10,510
Common Shareholders' Equity	3,841	4,670	6,888	8,531	10,510

Key Metrics

Net Interest Margin	5.94%	4.66%	4.86%	5.24%	4.99%
Tier 1 Ratio	16.2%	16.3%	16.4%	16.2%	16.0%
Effective Tax Rate	24.1%	20.0%	16.2%	20.0%	20.0%
Loan / Assets Ratio	47.1%	54.4%	59.7%	65.6%	70.9%
Loan / Deposit Ratio	75.1%	90.7%	102%	110%	118%
Oper Leverage (Inc Growth - Cost Growth)	5.16%	1.73%	37.3%	-13.3%	4.69%
Gearing (Assets / Equity)	9.48x	10.8x	8.99x	8.70x	8.44x
Tangible Equity / Assets	10.5%	9.29%	11.1%	11.5%	11.9%
Tangible Equity / WRAs	18.8%	17.1%	17.9%	17.4%	16.9%

Business Performance

Revenue Growth	25.8%	13.7%	59.2%	6.66%	16.3%
Operating Expense Growth	20.6%	12.0%	21.9%	19.9%	11.6%
Provisions Expense Growth	5.16%	-27.2%	-2.13%	53.1%	29.1%
Operating Revenue / Average Assets	3.02%	2.96%	4.97%	3.80%	3.75%
Operating Expenses / Average Assets	-4.17%	-3.38%	-3.18%	-3.14%	-2.93%
Pre-Provision ROA	4.45%	3.71%	5.54%	4.52%	4.52%
ROA	2.14%	2.26%	3.90%	2.87%	2.82%
Pre-Provision ROE	39.9%	37.8%	53.8%	39.9%	38.6%
ROE	19.3%	23.0%	37.8%	25.3%	24.1%
RoTE	19.8%	23.3%	38.1%	25.5%	24.2%
RoWRAs	3.91%	4.09%	6.65%	4.46%	4.12%
Dividend Payout Ratio	15.6%	10.7%	10.9%	16.2%	16.2%
Efficiency Ratio (Cost / Income Ratio)	48.4%	47.7%	36.5%	41.0%	39.4%

Quality of Earnings

Total Non-Interest Inc / Operating Inc	38.0%	38.1%	46.7%	34.3%	35.4%
Market-Related Revenue / Total Revenues	0%	0%	0%	0%	0%
Provisioning Burden as % of PPP	32.0%	20.2%	10.2%	15.8%	17.1%
NPLs plus Foreclosed Real Estate / Loans	4.17%	2.33%	2.37%	2.30%	2.40%
Loan Loss Reserves / NPLs	66.8%	70.8%	62.6%	70.0%	70.0%
Loan Loss Reserves / Total Loans	2.78%	1.65%	1.48%	1.61%	1.68%
Provisions Expense / Average Loans	3.23%	1.46%	0.99%	1.14%	1.13%

Company Description

Garanti Bank is one of Turkey's largest banks, but outside the top 3. Recently GE Consumer Finance took a stake in the bank, and we expect both to work closely on the domestic strengths in credit cards and mortgages, as well as future foreign expansion plans.

Stock Data

Price to Book Value 2.7x

Garanti Bank

We maintain our Buy recommendation for Garanti. Our PO at TRY12.4/share points to an upside of 40%. The stock is trading at only 8.0x 2009E P/E and 1.7x P/B.

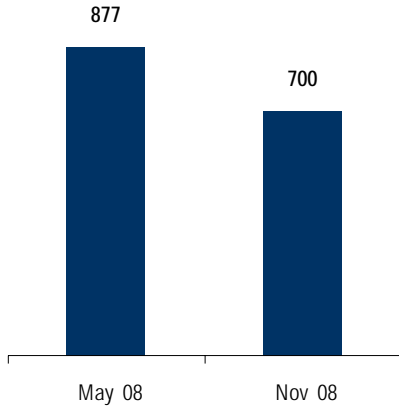
We expect Garanti to once again have beaten the competitors in growth in 2007 and continue to deliver a stronger growth in both 2008 and 2009. Our projections for loan growth are at 35% in 2007, 32% in 2008 and 29% in 2009.

The management's guidance for deposit growth is actually much higher than what we had forecasted earlier; we are raising deposit growth estimation in 2007 to 21% versus 18% earlier. For this year, we are pencilling in 22% rise. While these are the highest growth levels among competition, we believe it will be coming along with its costs. We expect to see the bank more aggressive in pricing its deposits throughout the year, as it has syndication rollovers of €600mn in May and US\$700mn in November. Based on this, we are lowering our 2008 NIM forecast to 5.2% from 5.6% earlier.

We expect Garanti to record the highest ROE in 2007 at 41% (29% adjusted for one off gains). Our ROE forecast for 2008 is at 27%.

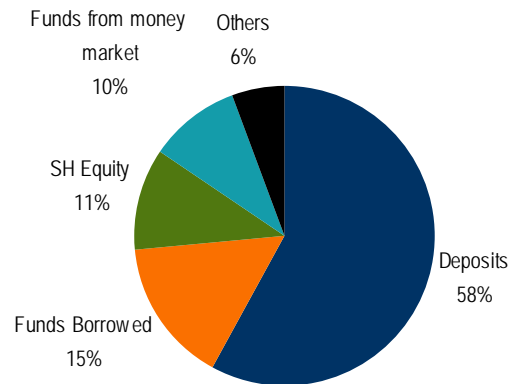
We are trying to make some sense out of the GE's 5% stake sale in Garanti with a 25% discount to the mcap. While this has now ended the equal stake partnership in the bank with the other partner Dogus, the management's guidance is still in favour of continuing cooperation in daily operations among the two parties. GE's comments also support Garanti management's wording on the issue but we cannot help but read the story as a possible change of heart for the partner's diminishing interest for Turkey. As this coincides with the upcoming Halkbank privatisation, it is also leading us to question how likely it is for Garanti to push the privatisation tender.

Chart 1: Syndications in 2008 (US\$mn)



Source: Garanti Bank

Chart 2: Liability breakdown at 9M 07



Source: Garanti Bank

Table 1: Forecasts

	TRYmn				y/y growth			
	2006	2007	2008	2009	06/05	07/06	08/07	09/08
Total Assets	50,287	61,902	74,247	88,674	38%	23%	20%	19%
Securities	14,395	15,148	15,714	16,119	26%	5%	4%	3%
Loans	27,350	36,985	48,690	62,840	59%	35%	32%	29.1%
Deposits	30,139	36,332	44,326	53,191	32%	21%	22%	20%
Borrowing	7,890	8,538	9,818	11,782	42%	8%	15%	20%
SH Equity	4,670	6,888	8,531	10,510	22%	47%	24%	23%
Net Int. Income	1,902	2,745	3,459	3,948	14%	44%	26%	14%
Net Fee Income	1,014	1,286	1,628	1,980	38%	27%	27%	22%
OPEX	1,465	1,785	2,141	2,390	12%	22%	20%	12%
Net Income	1,064	2,378	2,113	2,484	47%	124%	-11%	18%
Net income -adj	1,064	1,655				56%	28%	
NIM	4.7%	4.9%	5.2%	5.0%				
C/I	50%	45%	42%	40%				
Fees/OPEX	69%	72%	76%	83%				
ROE	25.0%	41.2%	27.4%	26.1%				
ROA	2.5%	4.2%	3.1%	3.0%				
Adj ROE		28.6%						
Adj ROA		3.0%						

Source: Merrill Lynch estimations; Garanti Bank

Price objective basis & risk

Garanti Bank (TKGBF)

We value Garanti Bank using a long-term dividend discount model. We used an initial cost of capital of 15.75% based on a risk free rate of 9.75%, equity risk premium of 5% and a beta of 1.2. Then assuming rates converging downwards, we gradually decrease our cost of capital to 10.75%. We use a terminal growth rate of 6%. This approach results in our price objective of TL12.10.

The risks to our price objective and assumptions are: (1) Turkey is not immune to global shocks; being an attractive carry trade market, a downturn in risk appetite would not be supportive of Turkish assets. (2) our assumptions are based on CBT cutting rates parallel to the disinflation environment; a reversal in sentiment would alter our forecasts. In terms of risks associated with Garanti Bank, its loan/deposit ratio above 100% may lead the bank to lower its growth targets or result in the bank easing its risk management requirements on running a short position.

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*iQmethod*SM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Amortization	Amortization
Operating Margin	Net Income	Shareholders' Equity
Earnings Growth	Operating Profit	Sales
Free Cash Flow	Expected 5-Year CAGR From Latest Actual	N/A
	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales}$	
	Other LT Liabilities	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

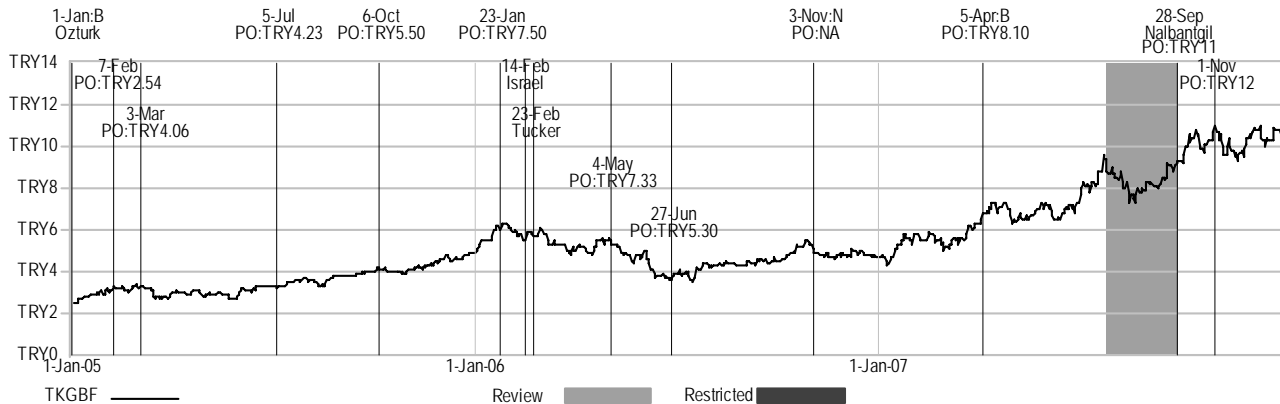
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TKGBF Price Chart



B : Buy, N : Neutral, S : Sell, PO : Price objective, NA : No longer valid

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark Grey shading indicates the security is restricted with the opinion suspended. Light Grey shading indicates the security is under review with the opinion withdrawn. Chart current as of December 31, 2007 or such later date as indicated.

Investment Rating Distribution: Banks Group (as of 01 Jan 2008)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	123	42.27%	Buy	49	49.00%
Neutral	129	44.33%	Neutral	63	57.27%
Sell	39	13.40%	Sell	25	67.57%

Investment Rating Distribution: Global Group (as of 01 Jan 2008)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1714	46.25%	Buy	445	29.10%
Neutral	1653	44.60%	Neutral	454	30.55%
Sell	339	9.15%	Sell	67	21.82%

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