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FIN322 Bank Management Written Project Assignment

Truist Financial Corp. (TFC) and US Bancorp (USB)

I. Executive summary

Truist Financial Corp- The company offers a wide range of services including retail, small business and commercial banking; asset management; capital markets; commercial real estate; corporate and institutional banking; insurance; mortgage; payments; specialized lending and wealth management. Truist conducts its business operations primarily through its bank subsidiary, Truist Bank, and other nonbank subsidiaries. Consumer banking and wealth creates 45% of total revenue while corporate and commercial banking creates about 50% and insurance holding creates the rest. TFC has various locations in the Southeastern and Mid-Atlantic United States. Revenue has grown nearly 30% in the past 5 years, but net income has seen some volatility. In 2019 TFC successfully merged with Suntrust.

US Bancorp- A diversified financial services company that provides lending and depository services, cash management, foreign exchange and trust and investment management services. The Company also provides credit card services, mortgage banking, insurance, brokerage, and leasing. It is the parent company of the U.S. Bank National Association, and is the fifth largest banking institution in the United States. Bancorp is headquartered in Minneapolis, Minnesota with just over 68,000 employees worldwide. They have sales of approximately $23 billion with $553 billion in assets and profits of $6 billion. US Bancorp's stock price was at its highest in July of 2021 at around $60 per share.

II. Capital Adequacy (Tier 1 and Total Capital ratios)

The tier 1 common equity ratio is found by dividing tier 1 capital less non-common elements, including qualifying preferred securities, by total risk-weighted assets. Tier 1 capital ratio is calculated by dividing tier 1 capital by total risk-weighted assets. The total capital ratio is computed by dividing total capital by total risk-weighted assets. These ratios are very important because they make sure banks have enough cushion to absorb a reasonable amount of losses before they become insolvent. This ensures the efficiency and stability of the financial system by lowering the risk of banks becoming insolvent. For example, higher capital adequacy ratios indicate the bank is safe and able to meet financial obligations.

<u>TFC:</u>

Tier 1 common equity ratio = 9.4%

Tier 1 capital ratio = 11%

Total capital ratio = 13%

USB:

Tier 1 common equity ratio = 9.8%

Tier 1 capital ratio = 11.5%

Total capital ratio = 13.4%

III. Earnings – Profitability (ROA, ROE NIM)

ROA, return on assets, is calculated by dividing net income by the firm's total assets. ROE, return on equity, is calculated by dividing net income by shareholder's equity. NIM, net interest margin, is calculated by dividing the difference between interest income and interest expense by the firm's assets. A firm with a higher ROA is always preferred because the firm can earn more money with a smaller investment. A "good" ROA is typically around 5%. A firm with a higher ROE efficiently uses its shareholder's equity to generate income and a "good" ROE is around 15-20%. NIM is the amount of money that a bank is earning in interest on loans compared to the amount it is paying in interest on deposits. The National average for NIM for US banks in 2021 was 2.49%.

TFC:

ROA = 1.07%   ROE = 9%   NIM = 2.86%

USB:

ROA = 1.35%   ROE = 14.1%   NIM = 2.56%

IV. Dividend Policy (Dividend Yield, Pay-Out Ratio)

The dividend yield is calculated by dividing the annual dividends paid per share by the price per share. The pay-out ratio is calculated by dividing total dividends paid out by net income.

TFC:

Dividend Yield = 3.78%   Pay-Out Ratio = 41.1%

USB:

Dividend Yield = 3.62%   Pay-Out Ratio = 42.21%

V. Rating Agency Ratings

TFC	S&P	Moody's	Fitch	DBRS Morningstar
Outlook/credit trend	Positive	Stable	Stable	Positive
Issuer	A- / A-2	A3	A+ / F1	AH / R-1L
Senior unsecured	A-	A3	A	AH
Subordinated	BBB+	A3	A-	A
Preferred Stock	BBB-	Baa2 (hyb)	BBB	BBBH

USB	S&P	Moody's	Fitch	DBRS Morningstar
Outlook / credit trend	Negative	Negative	Stable	Stable
Long term issuer	A+	A2	AA-	AA
Short term issuer	A-1	N/A	F1+	R-1 (middle)
Senior unsecured	A+	A2	A+	AA
Subordinated	A	A2	A	AA (low)
Junior subordinated	N/A	A3	N/A	N/A
Preferred Stock	BBB+	Baa1	BBB+	A
Commercial paper	N/A	P-1	F1+	N/A

VI. Stock Valuation PE, PEG

The price to earnings ratio, P/E ratio, is calculated by dividing the market price per share by the earnings per share (EPS). The price/earnings to growth ratio, PEG ratio, is calculated by dividing the P/E ratio by the annual EPS growth. The P/E ratio is the amount an investor can expect to invest in order to receive $1 of the firm's earnings. The P/E ratio is commonly used to help value a firm's stock and determine if it's over or underpriced. The PEG ratio is the correlation between the firm's market value and its projected earnings growth. A PEG higher than 1 is generally, but not always, considered unfavorable which means the stock may be overvalued.

<u>TFC:</u>

P/E = 9.07 PEG = 1.35

<u>USB:</u>

P/E = 10.73 PEG = 1.76

VII. Summary Analysis

It was difficult to choose one stock over the other because of how similar they are. Both banks have solid total capital ratios meaning they are well capitalized and able to meet financial obligations. USB has a higher ROA than TFC, but the difference is very small. However, USB is more efficient at using shareholder equity to generate income than TFC resulting in its ROE being 5.1 percentage points higher than TFC's ROE. The NIMs for both banks are very similar and close to the national average, but TFC's NIM is higher by 0.3 percentage points. The dividend yields and payout ratios are almost identical for both banks so that didn't affect our decision as much as these other metrics did. Both banks have similar credit ratings for debt like preferred stock, senior unsecured debt, and subordinated debt, but TFC was given a better outlook/credit trend by all four rating agencies. USB has a higher P/E and PEG ratio than TFC which could mean the stock is slightly more overvalued at the moment. After considering all of this information, we decided that today, it would be best to invest in USB because the bank has a better ROA and ROE. Since every other metric for the banks were so similar, we think that a higher ROA and ROE outweigh being a percentage point or two better in some of the other metrics we investigated.