



Bank of America (BAC)

Updated May 17th, 2018 by Jonathan Weber

Key Metrics

Current Price: \$31	5 Year CAGR Estimate: 11.5%	Quality Percentile: N/A
Fair Value Price: \$34	5 Year Growth Estimate: 8.2%	Momentum Percentile: N/A
% Fair Value: 92%	5 Year Valuation Multiple Estimate: 1.7%	Total Return Percentile: N/A
Dividend Yield: 1.6%	5 Year Price Target: \$50	Valuation Percentile:

Overview & Current Events

Bank of America provides all the traditional banking services as well as non-banking financial services. Its operations include Consumer Banking, Wealth & Investment Management and Global Banking & Markets. Bank of America was founded in 1904, is headquartered in Charlotte, NC, and is currently valued at \$315 billion, making it one of the biggest financial companies in the world.

Bank of America released its most recent earnings results on April 16. The company reported earnings per share of \$0.62, an increase of 38% over the prior year's quarter. Revenues totaled \$23 billion, an increase of four percent year over year.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$0.55	-	-	\$0.01	\$0.25	\$0.90	\$0.36	\$1.31	\$1.50	\$1.83	\$2.50	\$3.71
DPS	\$2.24	\$0.04	\$0.04	\$0.04	\$0.04	\$0.04	\$0.12	\$0.20	\$0.25	\$0.39	\$0.52	\$1.25

Bank of America's earnings and dividend history over the last decade doesn't look convincing at first sight. Both earnings and dividends were decimated during the last financial crisis, which made the share price drop substantially, whilst at the same time income investors' dividend stream all but stopped flowing. The last financial crisis was not a regular recession, though, thus a hit to Bank of America's profitability of that dimension is something very unusual.

Bank of America's profits have recovered nicely over the last couple of years, although the impact of the last financial crisis was clearly visible up to 2014. Going forward Bank of America should be able to remain on growth track, although the 38% earnings per share growth rate we have seen in the last quarter will not be the new standard.

In the coming years a couple of factors should provide earnings growth for Bank of America. The first is that the bank's loan portfolio keeps growing. During Q1 average loans grew by \$45 billion (5%) year over year. This loan growth is one component of a rising interest income, the other being rising interest rates. Banks are increasing the rate on loans at a faster pace than the rates they offer on deposits, which results in widening credit spreads. In a rising rate environment (as the one we are in right now) banks such as Bank of America are able to increase their net interest margin, together with a growing loan portfolio this poises well for the bank's net interest income, the main driver of higher earnings.

Bank of America also is, like other banks, focused on bringing down expenses, thereby raising margins. Its efficiency ratio improved by three percentage points during the last year, dropping to 50% (a lower efficiency ratio is better as it means the company's operating expenses are low relative to the revenues it generates). Last but not least the bank has been lowering its share count considerably over the last couple of years, in 2017 alone Bank of America has announced \$17 billion of buybacks – enough to repurchase 5% of the company's shares.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	---	---	---	---	---	15.0	---	12.6	10.3	13.5	12.4	13.5
Avg. Yld.	7.3%	0.3%	0.3%	0.4%	0.5%	0.3%	0.7%	1.2%	1.6%	1.6%	1.6%	2.5%

During the last financial crisis and in the following years Bank of America operated at a loss. This makes it difficult to put Bank of America's current valuation in a historic context (as its median PE ratio is 37). With a solid growth outlook and a healthy balance sheet (Bank of America has learned from its mistakes prior to the last financial crisis) it seems likely that shares will be valued at a low-teens earnings multiple.

Bank of America's dividend yield isn't very high right now, but the dividend growth rate has been quite high over the last couple of years, which is why the dividend yield will likely continue to rise going forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
Debt/A	90.1%	89.7%	90.3%	89.2%	89.1%	89.0%	88.6%	88.3%	87.7%	88.2%	87.9%	87.5%
Payout	---	---	---	---	16.0%	4.4%	33.3%	15.3%	16.7%	21.3%	20.8%	33.7%
Std. Dev.	70.4%	127%	31.6%	36.5%	45.5%	19.9%	18.8%	22.4%	21.7%	19.3%	21.0%	23.0%

In the above table we see that Bank of America's assets are financed via debt primarily, which isn't a surprise. Borrowing money and lending it to someone else at a higher rate is a bank's primary function. Bank of America's equity ratio has grown somewhat over the last decade, from 10% to 12%, which is a solid number for a bank. Bank of America's fully phased-in Basel 3 CET1 ratio is 11.4%, which shows that the bank is financed in a solid manner. The risk for another financial crisis is low, and credit quality at Bank of America is strong as well: During the most recent quarter the bank's net charge-off ratio declined to just 0.4%, which resulted in lower total charge-offs (\$900 million), despite the fact that the bank's loan portfolio has grown over the last year. The non-performing assets ratio has also declined over the last year, from 0.84% to 0.72%. Bank of America therefore looks like it is on solid financial ground, and it seems quite unlikely that investors will get burned again the same way as through the last financial crisis.

Bank of America competes with the biggest banks of the United States. Wells Fargo's (WFC) scandals that were uncovered over the last couple of years are a tailwind for Bank of America, as some customers are moving their accounts to Bank of America because of that (which explains why Bank of America's loan and deposits growth is faster than that of Wells Fargo). Bank of America also is the leader in online banking with more than 35 million active digital banking users and strong growth rates across its digital payments solutions.

Final Thoughts & Recommendation

During the last financial crisis Bank of America suffered greatly. The bank was unprofitable for years. With that said, the company has recovered. Bank of America looks quite strong now. The balance sheet is healthy, growth is solid and the company has amped up its shareholder returns. Bank of America could be a buy for investors looking for exposure to large US banks. Keep in mind, the stock is likely to perform poorly during the next recession, however.

Total Return Breakdown by Year

