Retirement Suitability Score

D

Unsuitable

Popular, Inc. (BPOP)

Updated September 30th, 2018 by Josh Arnold

Key Metrics

Current Price:	$51	**5 Year CAGR Estimate:**	8.6%	**Volatility Percentile:**	76.9%
Fair Value Price:	$64	**5 Year Growth Estimate:**	2.0%	**Momentum Percentile:**	91.8%
% Fair Value:	80%	**5 Year Valuation Multiple Estimate:**	4.6%	**Valuation Percentile:**	88.3%
Dividend Yield:	2.0%	**5 Year Price Target**	$69	**Total Return Percentile:**	55.1%

Overview & Current Events

Popular is a financial services company that traces its lineage back to the 1890's, when it was founded in Puerto Rico. The bank still calls the island home but has grown into several regions, including Central America, the Caribbean and the United States. Popular produces $1.7 billion in annual revenue and has a market capitalization of $5.2 billion.

Popular reported Q2 earnings on 7/23/18 and results were somewhat mixed. Adjusted earnings-per-share rose 33% against last year's Q2, driven by higher net interest income and expense leverage. The bank continues to see strong operating metrics, although some of them did slip against the comparable quarter. Net interest margin fell from 3.89% to 3.81% while provisions for loan losses rose, in addition to slightly lower equity totals on the balance sheet. Popular is still operating very efficiently but the slight deterioration of these core metrics has rightfully put a bit of a damper on what was a very strong quarter for revenue. We see earnings-per-share at $5.80 this year after Q2 results.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$25.50	$15.70	$6.60	$1.40	$2.35	$2.55	$2.38	$3.18	$2.04	$2.67	***$5.80***	***$6.25***
DPS	$4.80	$0.20	--	--	--	--	--	$0.15	$0.60	$0.90	***$1.00***	***$1.75***
Shares	28	64	102	103	103	104	104	104	104	102	***102***	***102***

Popular's earnings history is quite choppy, as one would imagine for a bank headquartered in Puerto Rico. The Great Recession took an obvious toll on earnings and the bank's capital levels, while the weak economic situation in its home country has crimped further earnings growth more recently. In total, we see modest 2% growth moving forward.

Popular continues to grab deposit market share and lend it prudently, leading to strong credit metrics. However, it appears credit quality may have plateaued, which removes a source of potential earnings growth, similar to many banks headquartered in the United States. Revenue should continue to climb at a low single digit rate but with net interest margin already near 4%, which is extraordinarily high compared to US banks, we see limited margin upside. Thus, despite Popular's operating metrics and prudent lending strategy, we see earnings growth as an uphill battle. It should be mentioned as well that Popular has nearly quadrupled its pre-Great Recession share count because it needed emergency capital and found it in the form of equity sales. This has kept a lid on earnings-per-share growth in the past decade as the share count mushroomed, and the new normal is going to be ~100 million shares.

The dividend was reinstated in 2015 after a years-long break after the Great Recession. It has since grown to $1.00 per share and we see continued growth in the payout as earnings have improved markedly. We are forecasting a dividend of $1.75 per share by 2023, which amounts to very respectable dividend growth from today's level.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	--	--	--	17.4	7.4	11.2	12.9	9.9	16.0	14.8	***8.8***	***11.0***
Avg. Yld.	5.4%	0.8%	--	--	--	--	--	0.5%	1.8%	2.5%	***2.0%***	***2.5%***

A spotty earnings history makes valuation analysis a bit tricky, but in recent years, the stock has traded with a low double-digit price-to-earnings multiple. Today, it stands at just 8.8, meaning we see the stock as offering good value against our fair value estimate of 11 times earnings. Uncertainty with Puerto Rico's economy may continue to weigh on the stock, but we see a 4.6% tailwind to total annual returns from a higher valuation. We also forecast the dividend yield to rise to 2.5% over time as the payout increases more quickly than the stock price.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
ROA	--	--	--	0.41%	0.67%	0.75%	0.76%	2.50%	0.56%	0.62%	***1.20%***	***1.20%***
Debt/A	92%	93%	90%	90%	89%	87%	87%	86%	87%	88%	***88%***	***88%***
LLP/Loans	4.0%	6.3%	3.8%	2.3%	1.6%	2.5%	1.3%	1.1%	0.7%	1.3%	**1.0%**	**0.9%**
Payout	19%	1%	--	--	--	--	--	5%	29%	34%	***17%***	***28%***
Std. Dev.	71%	125%	66%	44%	43%	38%	25%	21%	32%	24%	***25%***	***30%***

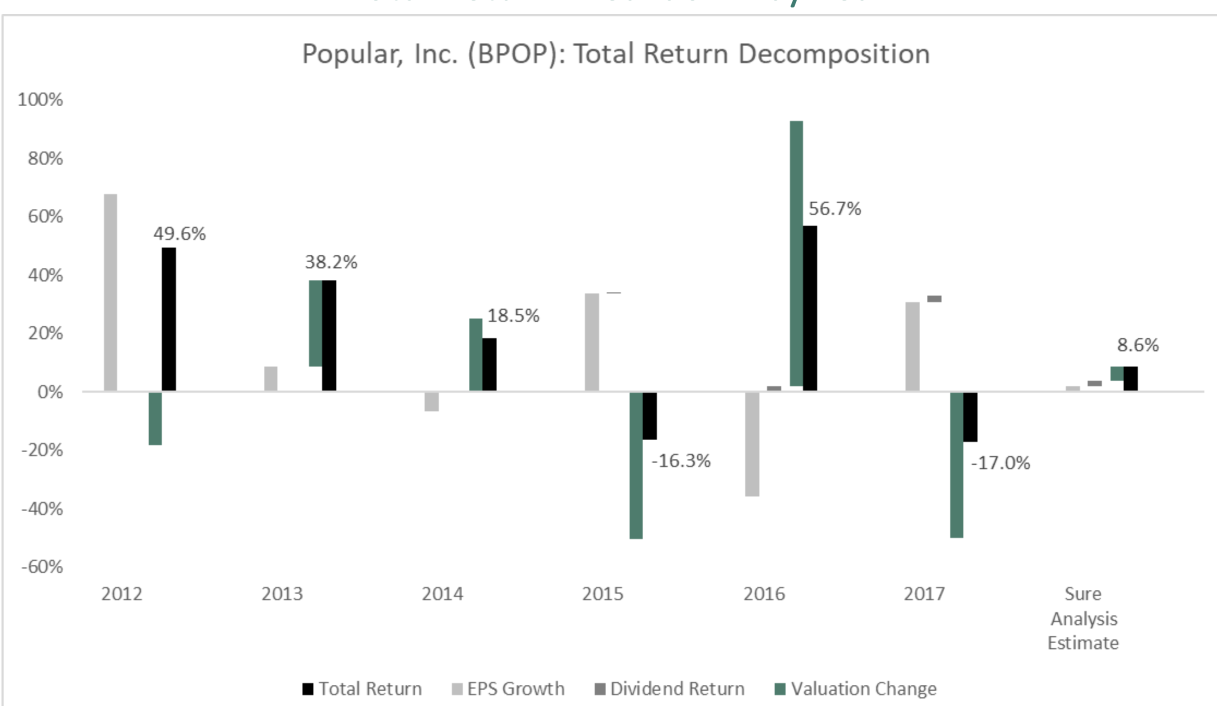
Popular's operating metrics have improved markedly since the depths of the Great Recession. Return on assets is around 1.2%, which is very high for a financial institution, while loan loss provisions have continued to improve and are now around 1% of total loans. We do not expect material deterioration in these key metrics, but the low-hanging fruit has certainly been picked. The payout ratio is still just 17% this year and we forecast it staying below 30% in the coming years, despite strong dividend growth. Popular likely wants to avoid another situation where it needs to cut the payout.

The bank's competitive advantage is in its enormous footprint in Puerto Rico and diversification in other countries in the region. Its balance sheet is also very strong, allowing for acquisitions and organic expansion. Recessions are not kind to Popular and the next one will almost certainly take a significant toll on earnings, which is true of almost any bank.

Final Thoughts & Recommendation

Overall, we see Popular as somewhat attractive given its favorable valuation and dividend growth prospects. We are forecasting total annual returns of 8.6%, consisting of 2% earnings growth, the 2% current yield and a 4.6% tailwind from a higher valuation. Popular would be attractive for dividend growth investors or those seeking value, but earnings growth looks to be limited. We rate Popular as a hold today given all of these factors. The company earns a D rating for retirement suitability, largely due to significant (~95%+) historical drawdowns in the price of its common stock.

Total Return Breakdown by Year



Click here to review the quality of this research report. Your feedback is important to us.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.