



# U.S. Bancorp (USB)

Updated January 19<sup>th</sup>, 2020 by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$55	<b>5 Year CAGR Estimate:</b>	6.6%	<b>Market Cap:</b>	\$86B
<b>Fair Value Price:</b>	\$49	<b>5 Year Growth Estimate:</b>	6.0%	<b>Ex-Dividend Date:</b>	03/28/20 <sup>1</sup>
<b>% Fair Value:</b>	112%	<b>5 Year Valuation Multiple Estimate:</b>	-2.2%	<b>Dividend Payment Date:</b>	04/15/20 <sup>2</sup>
<b>Dividend Yield:</b>	3.0%	<b>5 Year Price Target</b>	\$66	<b>Years Of Dividend Growth:</b>	9
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	B	<b>Last Dividend Increase:</b>	17.9%

## Overview & Current Events

U.S. Bancorp traces its lineage back to 1863 when the First National Bank of Cincinnati opened for business. It has since grown to 73,000 employees, an \$86 billion market capitalization, and \$23 billion in annual revenue. The bank has expanded from a regional player to a national powerhouse in recent years, becoming the fifth-largest bank by assets in the US. It competes mostly in traditional banking activities, but also offers wealth management, payment and investment services.

U.S. Bancorp reported Q4 and full-year earnings on January 15<sup>th</sup> and results missed expectations, sending the stock lower. Q4 net interest income was down -3% year-over-year in Q4 thanks to significantly lower net interest margin, which fell from 3.15% in last year's Q4 to 2.92% in this year's Q4. The bank's struggles with the compressed yield curve continue, and its investment portfolio suffered as well, along with the mix of earning assets the bank possessed.

Q4 noninterest income was down -2.5% year-over-year to \$2.44 billion, exacerbating the decline in net interest income. Average loans were essentially flat year-over-year just under \$300 billion, and average total deposits were up fractionally to \$357 billion. U.S. Bancorp's loan-to-deposit ratio of 83% is on the higher side of its large bank competitors, but certainly still has some upside potential to help return the bank to growth.

The net charge-off ratio also increased from 0.48% in this year's Q3 to 0.52%, indicating more deterioration in credit quality. While U.S. Bancorp's credit quality remains excellent, deterioration like this takes money directly out of earnings, as we saw in Q4.

Earnings-per-share came to \$1.08 on an adjusted basis in Q4, slightly missing the estimate of \$1.09, and down from \$1.10 in the year-ago quarter. Book value per share is also down from Q3, falling from \$30.26 to \$29.90.

We're out with an initial estimate of \$4.30 for 2020 earnings-per-share, reflecting continued yield curve challenges and relatively weak revenue growth.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$1.73	\$2.46	\$2.84	\$3.00	\$3.08	\$3.16	\$3.24	\$3.51	\$4.14	\$4.16	<b>\$4.30</b>	<b>\$5.75</b>
<b>DPS</b>	\$0.20	\$0.50	\$0.78	\$0.89	\$0.97	\$1.01	\$1.07	\$1.16	\$1.34	\$1.58	<b>\$1.68</b>	<b>\$2.25</b>
<b>Shares<sup>3</sup></b>	1,921	1,910	1,869	1,825	1,786	1,745	1,697	1,656	1,608	1,534	<b>1,500</b>	<b>1,425</b>

U.S. Bancorp's earnings-per-share history has been strong since the crisis ended, as it is one of very few banks to grow earnings every year since 2009. We expect U.S. Bancorp to see 6% annual earnings growth in the coming years.

It could achieve this by accruing the benefits of several tailwinds. First, it continues to grow its loan book at low single-digit rates. Second, net interest income continues to rise despite unfavorable rate movements, but U.S. Bancorp is slow to pass that benefit on to its depositors. Its rate on interest-bearing liabilities is rising with short-term rates but it is rising more slowly than U.S. Bancorp is increasing its average loan rate, boosting margins over time. Q4 saw a deviation

<sup>1</sup> Estimated date

<sup>2</sup> Estimated date

<sup>3</sup> Share count in millions

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from this, but we believe long-term margins are intact as yield curve inversions generally don't last very long. Third, it consistently repurchases its own stock, and we expect a low single-digit tailwind annually from buybacks.

U.S. Bancorp's payout ratio is in line with its peers and we expect growth in the payout to keep pace with earnings-per-share, growing to \$2.25 in five years. That would keep the payout ratio under 40% of earnings and in line with the bank's capital return strategy, affording it the opportunity to continue to buy back shares. With revenue and margin growth becoming tougher this late in the cycle, the buyback will take on increasing importance in the coming years.

## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	14.0	10.3	11.1	12.0	13.7	13.7	13.2	15.0	12.7	12.8	12.9	11.5
Avg. Yld.	0.8%	2.0%	2.5%	2.5%	2.3%	2.3%	2.5%	2.2%	2.6%	3.0%	3.0%	3.4%

U.S. Bancorp's price-to-earnings ratio has moved up in recent years as the bank has become more highly valued by investors than its competitors due to its outstanding profitability metrics. The valuation is in excess of our estimate of fair value at 11.5 earnings, so we see a modest headwind from the valuation in the coming years.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2019	2024
Payout	14%	22%	30%	32%	34%	34%	36%	36%	32%	38%	39%	39%

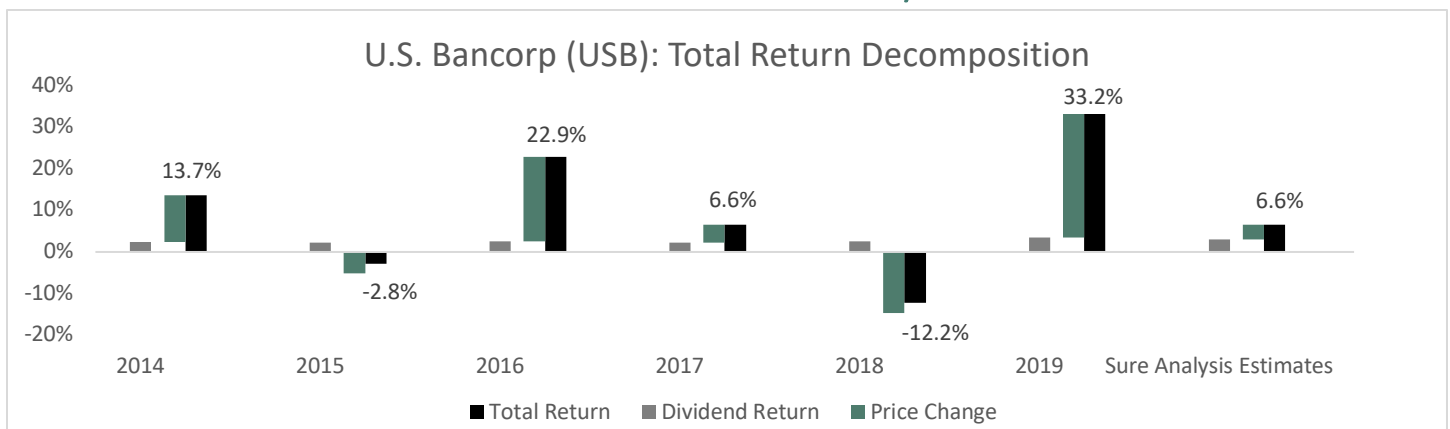
We see the payout remaining around 40% of earnings in the coming years after the recent increase, consistent with past years. U.S. Bancorp's dividend is very safe and we see no risk of a cut at this point. We forecast future growth in the payout as being roughly congruent with earnings expansion.

U.S. Bancorp's competitive advantage is in its stellar operating history and world-class management team. It operates as a regional bank, but on a massive scale, and as a result, it has been stronger through recessions than its larger peers. Indeed, earnings were not even cut in half in 2009 when many banks were struggling just to stay in business, and U.S. Bancorp came out of the recession in better shape in relation to its competitors than it was before the crisis.

## Final Thoughts & Recommendation

We continue to like U.S. Bancorp's fundamentals overall but note that total prospective returns have declined thanks to reduced growth estimates. We are expecting 6.6% annual returns moving forward, accruing from 6% earnings growth, the 3% current yield, and a modest headwind from the valuation. U.S. Bancorp continues to look attractive for a variety of investors, but we're reiterating our hold rating based upon total expected returns of under 7% per annum.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Revenue</b>	17939	18883	20064	19378	19939	20093	21105	21852	22521	22883
<b>SG&amp;A Exp.</b>	5878	6316	6778	7026	7137	7524	8032	8774	9124	9422
<b>D&amp;A Exp.</b>	596	565	561	520	501	481	470	468	467	
<b>Net Profit</b>	3317	4872	5647	5836	5851	5879	5888	6218	7096	6914
<b>Net Margin</b>	18.5%	25.8%	28.1%	30.1%	29.3%	29.3%	27.9%	28.5%	31.5%	30.2%
<b>Free Cash Flow</b>	5241	9820	7958	11446	5332	8782	5336	6472	10564	
<b>Income Tax</b>	935	1841	2236	2032	2087	2097	2161	1264	1554	1648

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Total Assets</b>	307.79	340.12	353.86	364.02	402.53	421.85	445.96	462.04	467.37	495.43
<b>Cash &amp; Equivalents</b>	14487	13962	8252	8477	10654	11147	15705	19505	21453	22405
<b>Goodwill &amp; Int.</b>	12167	11663	11849	12734	12551	12711	12647	12662	12761	12878
<b>Total Liab. (\$B)</b>	277.46	305.15	313.59	322.21	358.36	375.04	398.03	412.37	415.72	442.94
<b>Long-Term Debt</b>	64094	50740	42637	44276	59522	58216	46038	47855	52439	63890
<b>Total Equity</b>	27589	31372	34229	36357	38723	40630	41797	43621	45045	45869
<b>D/E Ratio</b>	2.17	1.49	1.09	1.08	1.37	1.26	0.97	0.98	1.03	1.23

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Return on Assets</b>	1.1%	1.5%	1.6%	1.6%	1.5%	1.4%	1.4%	1.4%	1.5%	1.4%
<b>Return on Equity</b>	12.7%	16.5%	17.2%	16.5%	15.6%	14.8%	14.3%	14.6%	16.0%	15.2%
<b>ROIC</b>	3.6%	5.4%	6.7%	6.9%	6.2%	5.6%	5.9%	6.5%	7.0%	6.3%
<b>Shares Out.</b>	1,921	1,910	1,869	1,825	1,786	1,745	1,697	1,656	1,608	1,534
<b>Revenue/Share</b>	9.34	9.82	10.58	10.48	11.00	11.34	12.24	12.98	13.75	14.46
<b>FCF/Share</b>	2.73	5.11	4.20	6.19	2.94	4.96	3.10	3.85	6.45	

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

### Disclaimer

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