Morgan Stanley (MS)

Updated December 7th 2020 by Nikolaos Sismanis

Key Metrics

Current Price:	$65	**5 Year CAGR Estimate:**	14.7%	**Market Cap:**	$117 B
Fair Value Price:	$74	**5 Year Growth Estimate:**	10.0%	**Ex-Dividend Date:**	01/30/2021
% Fair Value:	87%	**5 Year Valuation Multiple Estimate:**	2.8%	**Dividend Payment Date:**	02/14/2021
Dividend Yield:	2.2%	**5 Year Price Target**	$120	**Years Of Dividend Growth:**	7
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	16.7%

Overview & Current Events

Morgan Stanley is a financial holding company that provides various financial products and services to corporations, governments, financial institutions, and individuals worldwide. The company operates through Institutional Securities, Wealth Management, and Investment Management segments, including offering capital raising and financial advisory services, underwriting of debt, equity, and other securities, as well as advice on mergers and acquisitions. Morgan Stanley has a $117 billion market capitalization and is headquartered in New York, New York.

On October 15th, 2020, Morgan Stanley reported its Q3-2020 results for the quarter ending September 30th, 2020. The company achieved record Q3 revenues of $11.7 billion, a 16.7% increase year-over-year, and equally impressive EPS of $1.68, representing 31% growth vs. Q3-2019. Financials were boosted by all business segments growing. Investment management revenues, for instance, increased by 38%, driven by record inflows to assets amid the stock market's prolonged rally. Upon the company's recent acquisition of E-Trade, upgrade from Moody's, and the follow-up acquisition of Eaton Vance, management is expecting Morgan Stanley's financials to keep advancing higher due to operational efficiencies amid the various possible synergies.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$2.64	$1.25	-$0.02	$1.39	$1.64	$2.97	$2.98	$3.14	$4.81	$5.26	***$5.73***	***$9.23***
DPS	$0.20	$0.20	$0.20	$0.20	$0.40	$0.60	$0.75	$0.95	$1.15	$1.35	***$1.40***	***$2.06***
Shares[1]	1,361	1,654	1,885	1,905	1,924	1,909	1,849	1,780	1,708	1,617	***1,552***	***1,400***

Coming out of the Great Financial Crisis, Morgan Stanley's profitability has been expanding continuously, currently featuring a 5-year EPS CAGR of 14%. To adequately reward shareholders, management has been growing the company's DPS rapidly, by a CAGR of 30% over the same period.

The company's recent acquisitions of E-trade and Eaton Vance should not only achieve operational efficiencies as the company markets its services to a larger customer base with more assets under management, but its cash flow should become even more stable. Traditionally, banks like Morgan Stanley make money by the spread of lending rates and underwritings. However, both of these segments are subject to interest rates and the market's activity volume, respectively. The company's recent acquisitions should further transition Morgan Stanley's revenues into a more consistent stream, as both E-Trade and Eaton Vance charge their customers on a recurring basis, befitting from management fees.

It's worth mentioning that an additional boost to EPS and shareholder value creation has been Morgan Stanley's focus on buybacks. Management has taken advantage of the company's reasonable valuation to repurchase and retire nearly 20% of its shares outstanding since 2015.

Combining the company's recent robust performance, favorable EPS growth catalysts, including the recent acquisitions, as well as prudent focus on buybacks, we expect EPS and DPS growth of 10% and 8%, respectively, in the medium term.

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[1] Share count is in millions.

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	9.5	13.6	---	18.5	21.1	11.4	11.3	15.9	9.7	8.5	***11.3***	***13.0***
Avg. Yld.	0.8%	1.2%	1.1%	0.8%	1.2%	1.8%	2.2%	1.9%	2.5%	3.0%	***2.2%***	***1.7%***

Despite its solid profitability growth and aggressive capital returns, Morgan Stanley's valuation has remained quite reasonable throughout the decade. Shares are currently trading at around 11.3 times their expected FY2020 earnings. As buybacks continue and the company is seeing positive growth prospects in all its segments, we can see the stock's valuation multiple to expand to 13, better reflecting its two new subsidiaries and its overall robust performance. Combining our expected EPS growth being greater than DPS, and the stock's valuation expanding, its current yield of around 2.2% could move lower over time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

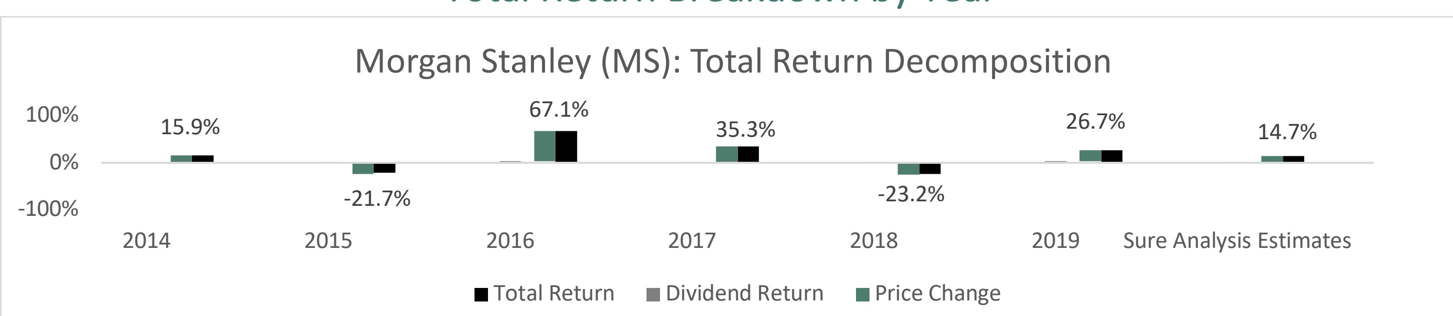
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	8%	16%	---	14%	24%	20%	25%	30%	24%	26%	***24%***	***22%***

Morgan Stanley's current dividend should be extremely safe, with a payout ratio under 25%. The company was previously forced to cut its dividend during the Great Financial Crisis. However, as its revenues have been transitioning continuously to the asset management side, we believe that the company's performance should be able to come out solid in a future potential recession. With global stimuli increasing demand for assets, Morgan Stanley's resiliency has been proven during the ongoing pandemic, not only by producing excellent financials but also by executing large acquisitions. Its competitive advantage lies in its sheer size, currently being the second-biggest wealth management firm in the U.S. only behind Bank of America. Finally, Morgan Stanley's greatest quality is most likely James Gorman, its CEO, who "single-handedly" transformed not only the company's operations but also culture since he took over in 2010, pivoting the company into a sustainably profitable one, with a proven focus towards creating shareholder value for the long-term. Still, the near-zero interest rate environment and massively competitive industry with consistently declining expense rates (e.g., near-zero fee ETFs) are two significant risks to keep in mind.

Final Thoughts & Recommendation

Led by a results-driven CEO, Morgan Stanley has successfully transformed into a thriving company in its industry, despite the heavy equity losses during the Great Financial Crisis. Its profitability as well as its capital returns which include its dividend growth and share buyback programs have been robust amid its growing operations, further displayed in the recent Q3 report. Summing our expected growth rates which include E-Trade's and Eaton Vance's operational synergies and the potential for a reasonable valuation multiple expansion due to its reasonable P/E ratio, we expect shares to deliver double-digit annualized returns in the medium-term, of around 14.7%. Shares earn a buy rating.

Total Return Breakdown by Year



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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.

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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	29,814	30,594	24,643	30,782	32,469	33,263	32,711	35,852	37,714	38,926
SG&A Exp.	18,082	18,727	18,128	18,683	20,117	18,464	18,252	19,566	20,339	21,691
D&A Exp.	1,419	1,404	1,581	1,511	1,161	1,433	1,736	1,753	1,844	2,643
Net Profit	4,703	4,110	68	2,932	3,467	6,127	5,979	6,111	8,748	9,042
Net Margin	15.8%	13.4%	0.3%	9.5%	10.7%	18.4%	18.3%	17.0%	23.2%	23.2%
Free Cash Flow	39,413	14,078	23,447	33,693	94	(5,836)	4,107	(6,134)	5,440	38,947
Income Tax	743	1,414	(161)	902	(90)	2,200	2,726	4,168	2,350	2,064

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets ($B)	808	750	781	833	802	787	815	852	854	895
Cash & Equiv.	66,795	76,766	77,874	99,086	87,591	54,083	43,381	46,164	51,840	49,659
Accounts Rec	54,150	43,421	64,288	57,104	48,961	45,407	46,460	56,187	53,298	55,646
Goodwill & Int.	11,406	10,971	10,433	9,881	9,747	9,568	9,298	9,045	8,851	9,250
Total Liab ($B)	742	680	716	764	729	711	738	773	772	813
Accounts Pay ($B)	3	124	128	157	181	187	191	191	180	198
LT Debt ($B)	206	187	172	156	155	156	166	193	190	193
Book Value	47,614	60,541	60,601	62,701	64,880	67,662	68,530	68,871	71,726	73,029
D/E Ratio	3.60	3.02	2.76	2.36	2.19	2.07	2.18	2.49	2.36	2.36

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	0.6%	0.5%	0.0%	0.4%	0.4%	0.8%	0.7%	0.7%	1.0%	1.0%
Return on Equity	11.1%	7.6%	0.1%	4.8%	5.4%	9.2%	8.8%	8.9%	12.4%	12.5%
ROIC	1.8%	1.6%	0.0%	1.3%	1.5%	2.7%	2.5%	2.4%	3.2%	3.3%
Shares Out.	1,361	1,654	1,885	1,905	1,924	1,909	1,849	1,780	1,708	1,617
Revenue/Share	21.13	18.26	12.84	15.73	16.47	17.03	17.33	19.69	21.70	23.74
FCF/Share	27.93	8.40	12.22	17.22	0.05	(2.99)	2.18	(3.37)	3.13	23.75

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