The Bank of New York Mellon Corp. (BK)

Updated January 21st, 2021 by Josh Arnold

Key Metrics

Current Price:	$42	**5 Year CAGR Estimate:**	8.3%	**Market Cap:**	$37.7 B
Fair Value Price:	$45	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	01/29/21
% Fair Value:	92%	**5 Year Valuation Multiple Estimate:**	1.6%	**Dividend Payment Date:**	02/12/21
Dividend Yield:	3.0%	**5 Year Price Target**	$55	**Years Of Dividend Growth:**	10
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	10.7%

Overview & Current Events

Bank of New York Mellon opened its doors in 1784 in the wake of the American Revolution, founded in part by Alexander Hamilton. The bank was the first ever to make a loan to the US government and in the nearly 240 years since, has grown to over $15 billion in annual revenue and a market capitalization of $38 billion. The bank is present in 35 countries around the world and acts as more of an investment manager than a traditional bank. Indeed, BNY Mellon's stated goal is help its customers manage their assets throughout the investment lifecycle. As such, BNY Mellon's revenue is mostly derived from fees, not traditional interest income.

Bank of New York Mellon reported fourth quarter and full year results on January 20th, 2021 and both revenue and adjusted earnings came in ahead of expectations. Total revenue was down -2% year-over-year to $3.9 billion; that number was fractionally higher than the third quarter of 2020. Net interest revenue was $683 million, down -3% quarter-over-quarter, and down -16% year-over-year. The more important fee and other revenue category was up 2% quarter-over-quarter, and up slightly year-over-year to $3.2 billion. The CEO noted that the company expects low interest rates will continue to be a headwind in 2021.

Assets under custody and/or administration was up 6% quarter-over-quarter and ended the year at $41.1 trillion. Assets under management rose nicely as well, adding 8% from the end of Q3 to $2.2 trillion. Provisions for credit losses were $15 million, up from $9 million in Q3, and up from a benefit of $8 million in the year-ago period.

Earnings-per-share came to $0.96 in Q4, down from $0.98 in both Q3 and the prior year Q4. Our initial estimate for this year is for $3.95 in earnings-per-share as we see rates as a major headwind, and modest growth in fee revenue.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$2.03	$2.03	$1.74	$2.41	$2.85	$3.17	$3.31	$4.21	$4.02	$4.01	***$3.95***	***$4.81***
DPS	$0.48	$0.52	$0.58	$0.66	$0.68	$0.72	$0.86	$1.04	$1.18	$1.24	***$1.24***	***$1.66***
Shares[1]	1,249	1,254	1,142	1,118	1,085	1,048	1,013	1,007	901	892	***870***	***800***

BNY Mellon's earnings-per-share were a bit underwhelming coming out of the crisis as they were roughly flat for six years. However, since 2013 BNY Mellon has fixed its efficiency issues, leading to better margins as it is now more prepared to take advantage of revenue increases. To that end, we are forecasting 4% earnings-per-share growth annually moving forward, although we note that earnings growth will likely to be tough to come by in 2021.

BNY Mellon can achieve this growth in a variety of ways. First, revenue continues to grow in the mid-single digits, something we expect to continue under normalized conditions. Its assets under custody and administration continue to grow over time, which is a key driver of fee income. Its lending business is small but growing and continues to add to top line growth as well, although this was not the case in 2020. We note that issues with AUM and lending margins tend to move in cycles, so BNY Mellon should see some respite from its headwinds over time. We also see the bank continuing its mid-single-digit pace of share repurchases over time, resulting in a meaningful tailwind for earnings-per-share outside

[1] Share count in millions

of revenue and dollar earnings growth. Finally, we expect margins to continue to improve slightly over time as the bank realizes additional operating leverage from higher revenue outpacing expense growth.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	12.4	11.2	17.2	15.1	14.5	12.7	15.1	12.6	11.9	9.6	***10.6***	***11.5***
Avg. Yld.	1.9%	2.3%	1.9%	1.8%	1.6%	1.8%	1.7%	2.0%	2.5%	3.2%	***3.0%***	***3.0%***

The stock's earnings multiple is now up to 10.6, but that is still below what we assess as fair value at 11.5 times earnings. Given this, we see a potential tailwind to total annual returns from the valuation in the coming years. We expect the dividend yield will be near 3% for the foreseeable future.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	24%	25%	34%	28%	27%	25%	29%	25%	29%	31%	***31%***	***35%***

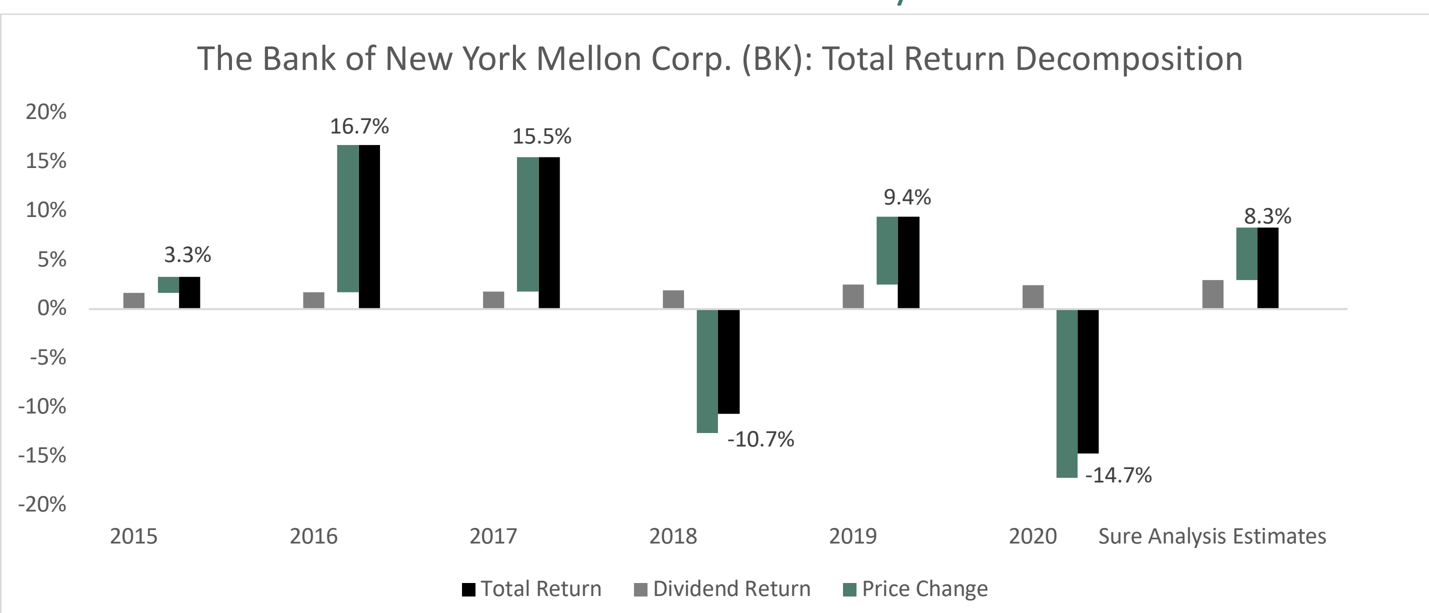
BNY Mellon's dividend is only about a third of its earnings, consistent with other large bank peers. That means the payout is very safe and we expect it to continue growing in the mid-single digits annually in the years to come.

BNY Mellon's competitive advantage is in its lack of reliance upon lending for revenue. This allows it to perform relatively well during recessions when other banks are struggling. While the company is not immune to downturns, its fee model is more resilient to such conditions than a bank that makes the majority of its revenue from interest income. Indeed, when many banks suffered in 2020, BNY Mellon saw essentially flat earnings year-over-year.

Final Thoughts & Recommendation

Overall, BNY Mellon looks like a cheaply valued stock with modest growth potential. We are forecasting total annual returns of 8.3% going forward, given the relatively low valuation, 3% yield, and moderate earnings growth when looking past 2021. The recent rally in the stock has brought it closer to our estimate of fair value, and as such, we are moving the stock down one notch from buy to hold.

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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	14,314	14,189	14,613	15,264	14,656	14,213	14,426	15,295	15,434	14,803
SG&A Exp.	5,987	6,036	6,336	6,113	6,104	6,054	6,262	6,373	6,276	6,071
D&A Exp.	776	1,246	1,389	1,292	1,457	1,502	1,474	1,339	1,315	---
Net Profit	2,516	2,437	2,104	2,567	3,158	3,547	4,090	4,266	4,441	3,617
Net Margin	17.6%	17.2%	14.4%	16.8%	21.5%	25.0%	28.4%	27.9%	28.8%	24.4%
Free Cash Flow	1,569	977	-1,251	3,693	3,526	5,442	3,470	4,888	-1,114	---
Income Tax	1,048	842	1,592	912	1,013	1,177	496	938	1,120	842

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets ($B)	325.3	359.0	374.5	385.3	393.8	333.5	371.8	362.9	381.5	469.6
Cash & Eq. ($B)	130.7	138.7	146.1	123.1	134.9	77.9	108.8	88.0	114.7	165.3
Acc. Receivable	4,868	4,848	4,100	4,773	4,097	4,628	5,200	4,363	4,426	510
Goodwill & Int.	24,042	24,001	23,776	23,328	22,815	22,365	22,474	22,222	22,083	20,508
Total Liab. ($B)	291.1	321.7	336.2	346.8	355.0	294.0	330.1	322.1	339.9	423.7
Long-Term Debt	22,117	20,248	20,623	21,050	22,070	25,217	34,082	34,329	32,059	26,334
Total Equity	33,417	35,363	35,935	35,879	35,485	35,269	37,709	37,096	37,941	41,260
D/E Ratio	0.66	0.56	0.55	0.56	0.58	0.65	0.83	0.84	0.77	0.58

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	0.9%	0.7%	0.6%	0.7%	0.8%	1.0%	1.2%	1.2%	1.2%	0.8%
Return on Equity	7.7%	7.1%	5.9%	7.1%	8.9%	10.0%	11.2%	11.4%	11.8%	9.1%
ROIC	4.6%	4.3%	3.6%	4.3%	5.2%	5.7%	5.8%	5.7%	6.0%	5.0%
Shares Out.	1,249	1,254	1,142	1,118	1,085	1,048	1,013	1,007	901	892
Revenue/Share	11.70	12.04	12.66	13.42	13.17	13.26	13.87	15.19	16.37	16.59
FCF/Share	1.28	0.83	(1.08)	3.25	3.17	5.08	3.34	4.85	(1.18)	---

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