# Prosperity Bancshares Inc. (PB)

*Updated February 1st, 2021 by Aristofanis Papadatos*

## Key Metrics

| | | | | | |
|---|---|---|---|---|---|
| **Current Price:** | $67 | **5 Year CAGR Estimate:** | 9.8% | **Market Cap:** | $6.2 B |
| **Fair Value Price:** | $82 | **5 Year Growth Estimate:** | 3.0% | **Ex-Dividend Date:** | 3/12/2021 |
| **% Fair Value:** | 81% | **5 Year Valuation Multiple Estimate:** | 4.2% | **Dividend Payment Date:** | 4/1/2021 |
| **Dividend Yield:** | 3.0% | **5 Year Price Target** | $95 | **Years Of Dividend Growth:** | 17 |
| **Dividend Risk Score:** | B | **Retirement Suitability Score:** | B | **Last Dividend Increase:** | 6.5% |

## Overview & Current Events

Prosperity Bancshares Inc. was formed in 1983 as a vehicle to acquire the former Allied Bank - chartered in 1949 as the First National Bank of Edna, Texas - which is now known as Prosperity Bank. The bank's main operation is receiving deposits from the general public and using the capital to originate commercial and consumer loans. The bank operates 261 branches in the greater Houston area and some neighboring counties in Texas and 14 more branches in Oklahoma. The company also has the following operations: wealth management, retail brokerage, and mortgage banking investment services. The bank's main lending focus is commercial mortgages, which make up 33% of their loan portfolio, followed by residential mortgages, which make up 24%. The company has a market capitalization of $6.2 billion.

On November 1st, 2019, Prosperity Bancshares completed the acquisition of LegacyTexas Bank in a deal valued at $2.1 billion. LegacyTexas has 42 branches in Texas and thus it has strengthened the position of Prosperity Bancshares in the area. As the deal value of $2.1 billion was almost half of the market cap of Prosperity Bancshares before the deal, it is evident that this acquisition is major for the future growth of Prosperity.

In late January, Prosperity Bancshares reported (1/27/21) financial results for the fourth quarter of fiscal 2020. In the year, loans grew 7.4%, deposits grew 13.1% and non-performing loans remained low, at 0.20% of interest-earning assets. Moreover, the company grew its earnings-per-share 26%, primarily thanks to the integration of LegacyTexas Bank, and thus achieved all-time high earnings-per-share. The bank has some exposure to the energy sector, which has been severely hit by the coronavirus crisis. However, it expects negligible losses from these loans. Moreover, Prosperity Bancshares has a reputation for its disciplined management and hence we expect it to endure the ongoing recession without any problem. Its record earnings in 2020 and its recent 6.5% dividend raise are testaments to the resilience of this bank to downturns.

## Growth on a Per-Share Basis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **EPS** | $3.01 | $3.23 | $3.65 | $4.32 | $4.09 | $3.94 | $3.92 | $4.61 | $4.52 | $5.68 | ***$5.75*** | ***$6.67*** |
| **DPS** | $0.72 | $1.00 | $0.65 | $0.99 | $1.12 | $1.24 | $1.38 | $1.49 | $1.64 | $1.87 | ***$2.00*** | ***$2.60*** |
| **Shares[1]** | 46.9 | 56.5 | 66.1 | 69.8 | 70.0 | 69.5 | 69.5 | 69.9 | 94.7 | 92.6 | ***92.0*** | ***90.0*** |

Prosperity Bancshares has grown its earnings-per-share at a 7.3% average annual rate in the last decade, primarily thanks to strong economic activity in Texas and Oklahoma. The bank stalled from 2014 to 2017 but it has reignited growth in the last three years. In addition, the pandemic has not disrupted the growth trajectory of the company, primarily thanks to its recent major acquisition and the resultant synergies. Due to the all-time high earnings expected in 2021, we expect the bank to grow its earnings-per-share by 3.0% per year on average over the next five years. The bank initiated a quarterly dividend of $0.025 per share in January-1999 and has grown it at a fast clip to $0.49 per quarter. In the last five years, the bank has raised its dividend by 9.6% per year on average. Thanks to its low payout ratio (35%) and its promising growth prospects, the company should be able to continue raising its dividend at a healthy pace.

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[1] In millions.

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## Valuation Analysis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Now | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Avg. P/E** | 13.4 | 12.7 | 17.2 | 12.9 | 11.8 | 18.3 | 17.7 | 13.5 | 15.4 | 10.5 | ***11.7*** | ***14.3*** |
| **Avg. Yld.** | 1.8% | 2.3% | 1.2% | 1.7% | 2.1% | 2.4% | 2.1% | 2.1% | 2.4% | 3.1% | ***3.0%*** | ***2.7%*** |

Prosperity Bancshares is currently trading at a price-to-earnings ratio of 11.7, which is much lower than its 10-year average earnings multiple of 14.3, primarily due to the underperformance of the entire financial sector during the pandemic. If the stock reverts to its average valuation level over the next five years, it will enjoy a 4.2% annualized gain in its returns.

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

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Payout** | 24% | 25% | 24% | 23% | 27% | 31% | 35% | 32% | 36% | 33% | ***35%*** | ***39%*** |

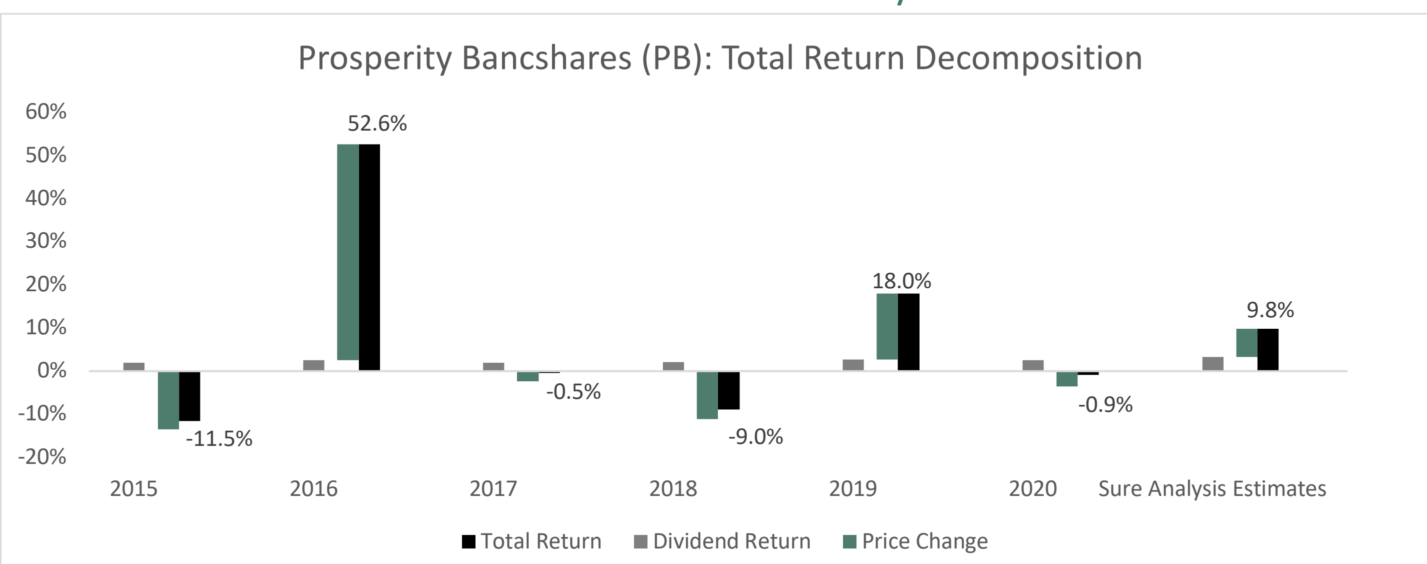
Prosperity Bancshares believes that its competitive advantage is in its presence in areas with strong economic growth and excellent growth opportunities through acquisitions, new banking center locations and business development.

A risk for Prosperity is the current recession in the U.S. economy, which has been caused by the pandemic. The company could experience increased loan and lease charge-offs, though such charges have been very limited so far. Although this economic downturn is a risk for Prosperity Bank, the bank was able to grow immensely in the last recession. During the Great Recession (2008-2009), its stock rallied 36% throughout the year despite a declining broad market. The company was also able to grow its earnings-per-share by an outstanding 29% and its book value per share by nearly 7%. The bank is proving resilient in the ongoing recession as well, as it achieved record earnings-per-share in 2020.

## Final Thoughts & Recommendation

Prosperity Bancshares is facing a headwind from the pandemic, but it is conservatively managed and hence we expect it to outperform its peers, just like it did in the Great Recession. The bank has rallied 22% since our previous report, in November, but it remains attractive. Thanks to its cheap valuation, the stock could offer a 9.8% average annual return over the next five years. We thus maintain our 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 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Revenue** | 376 | 447 | 582 | 776 | 736 | 734 | 716 | 728 | 796 | 1,122 |
| **SG&A Exp.** | 112 | 138 | 177 | 236 | 228 | 232 | 227 | 241 | 256 | 332 |
| **D&A Exp.** | 16 | 16 | 17 | 24 | 22 | 22 | 19 | 18 | 20 | --- |
| **Net Profit** | 142 | 168 | 221 | 297 | 287 | 274 | 272 | 322 | 333 | 529 |
| **Net Margin** | 37.7% | 37.6% | 38.0% | 38.3% | 39.0% | 37.4% | 38.0% | 44.2% | 41.8% | 47.1% |
| **Free Cash Flow** | 208 | 197 | 284 | 336 | 301 | 329 | 379 | 305 | 384 | --- |
| **Income Tax** | 72 | 84 | 108 | 148 | 144 | 134 | 134 | 81 | 87 | 116 |

## Balance Sheet Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Total Assets** | 9823 | 14584 | 18642 | 21508 | 22037 | 22331 | 22587 | 22693 | 32186 | 34059 |
| **Cash & Equivalents** | 213 | 326 | 381 | 677 | 563 | 436 | 392 | 411 | 574 | 1343 |
| **Accounts Receivable** | 29 | 42 | 49 | 52 | 52 | 53 | 56 | 57 | 81 | --- |
| **Goodwill & Int. Ass.** | 946 | 1243 | 1714 | 1933 | 1918 | 1947 | 1940 | 1934 | 3310 | 3305 |
| **Total Liabilities** | 8255 | 12494 | 15855 | 18263 | 18574 | 18689 | 18763 | 18641 | 26215 | 27929 |
| **Accounts Payable** | 3 | 2 | 3 | 3 | 2 | 2 | 3 | 4 | 9 | --- |
| **Long-Term Debt** | 98 | 342 | 135 | 176 | 491 | 991 | 505 | 1031 | 1430 | --- |
| **Shareholder's Equity** | 1567 | 2089 | 2787 | 3245 | 3463 | 3642 | 3824 | 4053 | 5971 | 6131 |
| **D/E Ratio** | 0.06 | 0.16 | 0.05 | 0.05 | 0.14 | 0.27 | 0.13 | 0.25 | 0.24 | --- |

## Profitability & Per Share Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Return on Assets** | 1.5% | 1.4% | 1.3% | 1.5% | 1.3% | 1.2% | 1.2% | 1.4% | 1.2% | 1.6% |
| **Return on Equity** | 9.4% | 9.2% | 9.1% | 9.9% | 8.5% | 7.7% | 7.3% | 8.2% | 6.6% | 8.7% |
| **ROIC** | 7.9% | 8.2% | 8.3% | 9.4% | 7.8% | 6.4% | 6.1% | 6.8% | 5.3% | 7.8% |
| **Shares Out.** | 46.9 | 56.5 | 66.1 | 69.8 | 70.0 | 69.5 | 69.5 | 69.9 | 94.7 | 92.6 |
| **Revenue/Share** | 7.99 | 8.60 | 9.61 | 11.26 | 10.50 | 10.53 | 10.31 | 10.42 | 10.83 | 12.06 |
| **FCF/Share** | 4.43 | 3.80 | 4.68 | 4.88 | 4.30 | 4.73 | 5.46 | 4.37 | 5.23 | --- |

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