The Bank of New York Mellon Corp. (BK)

Updated April 21st, 2022, by Josh Arnold

Key Metrics

Current Price:	$47	**5 Year CAGR Estimate:**	9.8%	**Market Cap:**	$37 B
Fair Value Price:	$55	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	04/27/22
% Fair Value:	85%	**5 Year Valuation Multiple Estimate:**	3.3%	**Dividend Payment Date:**	05/11/22
Dividend Yield:	2.9%	**5 Year Price Target**	$67	**Years Of Dividend Growth:**	11
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Rating:**	Hold

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 U.S. government and in the nearly 240 years since, has grown to nearly $17 billion in annual revenue and a market capitalization of $37 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.

BNY Mellon posted first quarter earnings on April 18th, 2022, and results were almost exactly in line with estimates on both the top and bottom lines. Earnings-per-share came to 86 cents, which was one penny better than expected. Revenue was up fractionally year-over-year to $3.93 billion, but missed estimates by just $10 million.

Average assets under custody soared 9% year-over-year to $45.5 trillion, while assets under management rose 2% to $2.3 trillion. The bank also posted a $2 million provision for credit losses, which was a sharp decline from the net benefit of $83 million a year ago. We note that enormous COVID-related provisions were being unwound in last year's Q1, so this year's Q1 is a much better picture of a normalized result.

Capital remains strong with a common equity tier 1 ratio of 10.1%, and a tier 1 leverage ratio of 5.3%. BNY Mellon remains well capitalized.

Total revenue would have risen 2% year-over-year without the impact of the company's exposure to Russia. Net interest revenue was $701 million, up from $681 in Q4 and up from $655 million in last year's Q1. Net interest margin was 76 basis points, up from 71 bps in Q4 and 67 bps a year ago.

Noninterest expense was $3.01 billion, up slightly from $2.97 billion in Q4, and up from $2.85 billion in the year-ago period. The increase was due to staff expense increases.

Our estimate of earnings-per-share for this year is essentially unchanged after Q1 results at $4.60, which we note would be a record for BNY Mellon if achieved.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$2.03	$1.74	$2.41	$2.85	$3.17	$3.31	$4.21	$4.02	$4.01	$4.18	***$4.60***	***$5.60***
DPS	$0.52	$0.58	$0.66	$0.68	$0.72	$0.86	$1.04	$1.18	$1.24	$1.33	***$1.36***	***$1.74***
Shares[1]	1,254	1,142	1,118	1,085	1,048	1,013	1,007	901	879	826	***790***	***700***

BNY Mellon's earnings-per-share were a bit underwhelming coming out of the financial 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.

[1] Share count in millions

BNY Mellon can achieve this growth in a variety of ways. First, revenue continues to grow over time, something we expect to continue under normalized conditions. Its assets under custody and administration continue to grow as well, particularly during strong equity markets, 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 share repurchases over time, resulting in a meaningful tailwind for earnings-per-share outside of revenue and company-wide 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. Investors would do well to continue to monitor expense growth against revenue growth for signs of margin deterioration.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	11.2	17.2	15.1	14.5	12.7	15.1	12.6	11.9	9.6	12.2	***10.2***	***12.0***
Avg. Yld.	2.3%	1.9%	1.8%	1.6%	1.8%	1.7%	2.0%	2.5%	3.2%	2.6%	***2.9%***	***2.6%***

The stock's earnings multiple is now just 10.2, well under our estimate of fair value at 12 times earnings. Given this, we see a modest tailwind to total returns in the coming years from the valuation. We expect the dividend yield will be under 3% for the foreseeable future.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	25%	34%	28%	27%	25%	29%	25%	29%	31%	32%	***30%***	***31%***

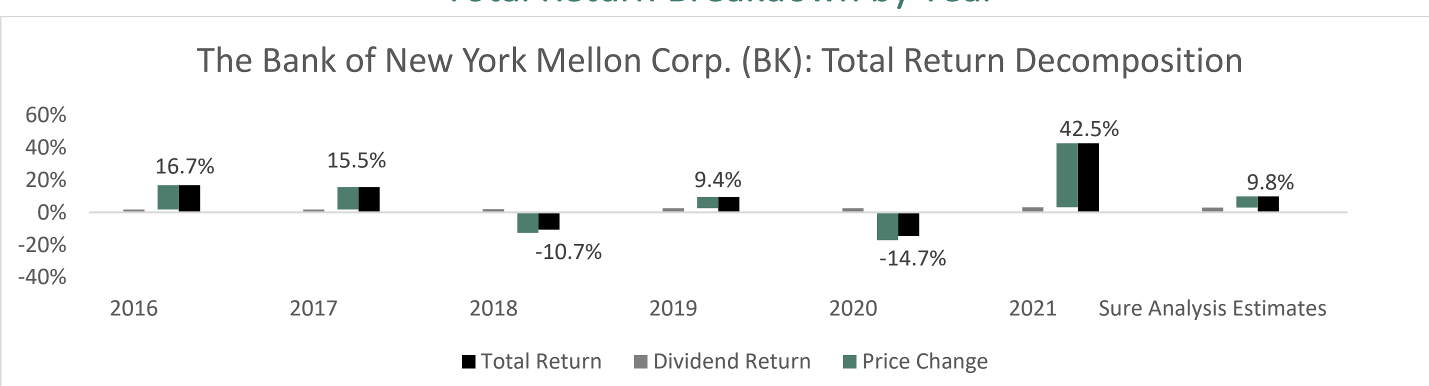
BNY Mellon's dividend is only about a third of its earnings, consistent with other large bank peers. That means the payout is very safe and we expect it to continue growing in the mid-single digits annually in the years to come.

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 an undervalued stock with modest growth potential. We are forecasting total annual returns of 9.8% going forward, given the valuation, 2.9% yield, and moderate earnings growth from what should be a fairly high base for 2022. We reiterate the stock at a hold rating following Q1 results.

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	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	14,189	14,613	15,264	14,656	14,213	14,426	15,295	15,434	15,472	15,633
SG&A Exp.	6,036	6,336	6,113	6,104	6,054	6,262	6,373	6,276	5,966	6,337
D&A Exp.	1,246	1,389	1,292	1,457	1,502	1,474	1,339	1,315	1,630	1,867
Net Profit	2,437	2,104	2,567	3,158	3,547	4,090	4,266	4,441	3,617	3,759
Net Margin	17.2%	14.4%	16.8%	21.5%	25.0%	28.4%	27.9%	28.8%	23.4%	24.0%
Free Cash Flow	977	-1,251	3,693	3,526	5,442	3,470	4,888	-1,114	3,816	1,623
Income Tax	842	1,592	912	1,013	1,177	496	938	1,120	842	877

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets ($B)	359.0	374.5	385.3	393.8	333.5	371.8	362.9	381.5	469.6	444.4
Cash & Eq. ($B)	138.7	146.1	123.1	134.9	77.9	108.8	88.0	114.7	162.1	121.3
Acc. Receivable	4,848	4,100	4,773	4,097	4,628	5,200	4,363	4,426	4,129	4,635
Goodwill & Int.	24,001	23,776	23,328	22,815	22,365	22,474	22,222	22,083	22,392	22,599
Total Liab. ($B)	321.7	336.2	346.8	355.0	294.0	330.1	322.1	339.9	423.5	401.0
Long-Term Debt	20,248	20,623	21,050	22,070	25,217	34,082	34,329	32,059	26,334	26,680
Total Equity	35,363	35,935	35,879	35,485	35,269	37,709	37,096	37,941	41,260	38,196
LTD/E Ratio	0.56	0.55	0.56	0.58	0.65	0.83	0.84	0.77	0.58	0.62

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.7%	0.6%	0.7%	0.8%	1.0%	1.2%	1.2%	1.2%	0.8%	0.8%
Return on Equity	7.1%	5.9%	7.1%	8.9%	10.0%	11.2%	11.4%	11.8%	9.1%	9.5%
ROIC	4.3%	3.6%	4.3%	5.2%	5.7%	5.8%	5.7%	6.0%	4.9%	5.3%
Shares Out.	1,254	1,142	1,118	1,085	1,048	1,013	1,007	901	892	856
Revenue/Share	12.04	12.66	13.42	13.17	13.26	13.87	15.19	16.37	17.34	18.26
FCF/Share	0.83	(1.08)	3.25	3.17	5.08	3.34	4.85	-1.18	4.28	1.90

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