Banco Santander (SAN)

Updated May 20th, 2022, by Josh Arnold

Key Metrics

Current Price:	$2.89	**5 Year CAGR Estimate:**	7.5%	**Market Cap:**	$48 B
Fair Value Price:	$3.23	**5 Year Growth Estimate:**	2.0%	**Ex-Dividend Date:**	10/28/2022[1]
% Fair Value:	90%	**5 Year Valuation Multiple Estimate:**	2.2%	**Dividend Payment Date:**	11/04/2022
Dividend Yield:	3.8%	**5 Year Price Target**	$3.56	**Years Of Dividend Growth:**	1
Dividend Risk Score:	D	**Retirement Suitability Score:**	C	**Rating:**	Hold

Overview & Current Events

Banco Santander, headquartered in Madrid, Spain, is a diversified banking business with operations in Retail Banking, Santander Corporate and Investment Banking, Wealth Management, and Spain Real Estate Activity. The company is truly global, with a presence in Europe, North America, and South America. Santander's top markets by attributable profit include Brazil (26% of profit), Spain (17%), The United Kingdom (13%), Santander Consumer Finance (13%), Mexico (8%), Chile (6%), USA (5%), Portugal (5%), Poland (3%) and Argentina (1%). The $48 billion market capitalization company has 11,200 branches, with 198,000 employees serving tens of millions of customers around the globe. Santander reports results in euro, but all numbers for this report are in U.S. dollars.

Santander reported first quarter earnings on April 26th, 2022, and results were somewhat better than expected. However, management was forthcoming with commentary and guidance that suggested some challenges were ahead, and the stock traded lower on the report.

Management said that this year should see mid-single digit revenue growth, a 45% efficiency ratio, and capital returns of 40% of underlying profit to shareholders through dividends and buybacks in equal amounts.

Santander posted a 9.4% gain in underlying, before-tax profit from the year-ago period. Net interest income was $9.45 billion in Q1, up 1.6% quarter-over-quarter, and up 11.3% year-over-year. Fee income in Q1 was up 4.5% Q/Q and up 10.4% Y/Y. Total revenue was up 8% year-over-year in Q1. Management noted that costs rose 4% in constant euros, but accounting for inflation, costs fell 3% on Santander's continued productivity improvement across its markets. Santander's exposure to South America and its high rates of inflation are driving cost increases.

Following Q1 results, we've trimmed our estimate for earnings-per-share to 43 cents, and following the first dividend announcement, we now see 11 cents per share paid out rather than 12.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$0.29	$0.54	$0.64	$0.45	$0.45	$0.46	$0.53	$0.52	$0.32	$0.53	***$0.43***	***$0.47***
DPS	$0.79	$0.83	$0.73	$0.22	$0.22	$0.26	$0.27	$0.26	---	$0.06	***$0.11***	***$0.12***
Shares[2]	10,321	11,333	12,584	14,434	14,582	16,136	16,237	16,618	17,312	17,063	***17,000***	***17,000***

Note that all the numbers in this report refer to the Banco Santander American Depository Receipts (ADRs) in USD, listed on the NYSE (ticker: SAN). Keep in mind that the Euro to USD exchange rate has varied over this time. Today, the exchange rate is 1.06 USD per Euro. The company had traditionally paid three cash dividends and one scrip dividend each year (which is why the share count rises over time). However, recent restrictions put into place by regulators have changed that, and the future of the company's share repurchases, and dividends is in some measure of doubt today. The dividend has been restarted, but it is quite variable in both amount and timing, and therefore difficult to predict.

Santander's Latin America markets have higher growth rates than their European counterparts. Of course, this is also a point of risk as these markets are not as established and overall credit tends to be more finicky. Due to extremely low

[1] Estimated date

[2] Share count in millions

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.

rates around the world, as well as high inflationary pressures in many of Santander's markets, we are reiterating our growth forecast of 2% annually. Santander continues to struggle with rates and credit quality to an extent, and we don't see that changing given its focus on auto loan origination.

The early-2022 acquisition of Santander Consumer USA should help fuel consumer loan growth in the US in the years to come as well after synergies can begin to be realized.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	27.8	16.6	13.3	11.0	11.6	14.3	8.5	8.5	8.3	6.8	***6.7***	***7.5***
Avg. Yld.	9.8%	9.3%	8.6%	4.4%	4.2%	4.0%	6.0%	5.9%	---	1.6%	***3.8%***	***3.4%***

Santander has somewhat of a peculiar trading history, as the dividend was held relatively steady for years even after earnings collapsed. Eventually, the high dividend payment caught up with the firm and a dividend cut was required. As mentioned, the cash dividend was suspended for 2020. The dividend is back, but we note the payout is variable.

Since the dividend cut shares have been trading in a more normalized range. Our fair value estimate is 7.5 times earnings, due to the obvious growth struggles the company is facing, in addition to the lateness of the global economic cycle. With shares trading at 6.7 times our earnings estimate, we see a small tailwind on total returns in the coming years from the valuation.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	272%	154%	114%	49%	49%	57%	51%	50%	---	11%	***26%***	***26%***

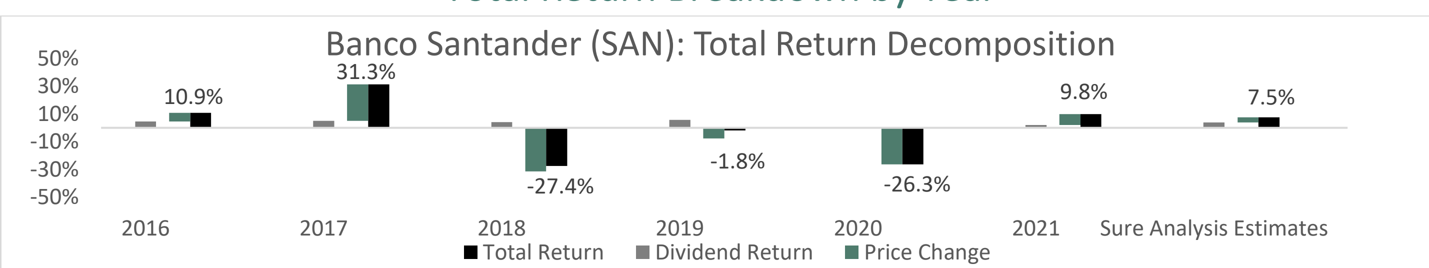
Santander has a few advantages over a typical bank, stemming from its top-five deposit market share in countries like Spain, Brazil, Mexico, Chile, and Argentina. The wide geographical base gives the company multiple positions in markets that are not necessarily correlated.

Recession performance and its aftermath are noteworthy. Santander went from earning $1.79 per share in 2008 down to $0.84 in 2011 and $0.29 in 2012. Since then, earnings had rebounded, but not nearly to the same level. We believe Santander should have slashed the dividend much earlier. Despite the material and lasting impact to earnings, the dividend continued along until 2014. Those four years of a near (or well above) 100% payout ratio required significant dilutive action. We see 2020's recession as damaging as well, but a rather swift recovery into 2021 has given way to what should be normalized earnings for 2022.

Final Thoughts & Recommendation

We are forecasting 7.5% annual total returns going forward. We see Santander as a hold due to unattractive growth prospects, but a decent projected yield. Santander is a risky bank to own, but the tailwind from the valuation, and the nearly-4% yield are attractive.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	65,553	62,795	62,893	52,610	50,608	56,762	58,703	58,574	53,461	57,323
SG&A Exp.	28,713	28,705	23,188	20,832	20,202	22,443	23,377	22,118	20,922	22,077
D&A Exp.	2,807	3,175	3,041	2,683	2,616	2,937	2,863	3,360	3,209	3,261
Net Profit	2,935	5,545	7,734	6,620	6,866	7,496	9,222	7,294	-10,017	9,612
Net Margin	4.5%	8.8%	12.3%	12.6%	13.6%	13.2%	15.7%	12.5%	-18.7%	16.8%
Free Cash Flow	26,029	-50,458	-20,055	-3,948	14,923	35,334	-10,366	-12,039	65,818	53,584
Income Tax	751	2,701	4,944	2,456	3,632	4,399	5,769	4,956	6,432	5,790

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets ($B)	1679	1541	1540	1465	1416	1733	1669	1706	1855	1807
Cash & Eq. ($B)	157	107	102	105	104	164	160	144	213	320
Goodwill & Int.	37112	36235	36968	32176	31103	34411	32670	31014	19,566	18,777
Total Liab. ($B)	1572	1431	1431	1357	1307	1605	1546	1582	1,743	1,697
Accounts Payable	1926	1692	1786	---	1491	2218	1814	1891	2,457	2,717
LT Debt ($B)	297	265	260	247	242	261	282	293	289	279
Total Equity ($B)	95	97	98	96	96	113	110	112	100	98
LTD/E Ratio	3.12	2.72	2.64	2.57	2.52	2.31	2.56	2.62	2.89	2.83

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.2%	0.3%	0.5%	0.4%	0.5%	0.5%	0.5%	0.4%	-0.6%	0.5%
Return on Equity	3.1%	5.8%	7.9%	6.8%	7.1%	7.2%	8.2%	6.6%	-9.4%	9.7%
ROIC	2.2%	4.2%	6.4%	6.1%	6.3%	6.3%	7.3%	5.9%	-2.4%	2.4%
Shares Out.	10,321	11,333	12,584	14,434	14,582	16,136	16,237	16,618	17,312	17,063
Revenue/Share	6.57	5.72	5.64	3.72	3.57	3.84	3.19	2.80	3.28	3.08
FCF/Share	2.65	-4.63	-1.69	-0.27	1.02	2.29	-0.64	-0.73	4.04	3.09

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