



The Bank of New York Mellon Corp. (BK)

Updated July 18th, 2022, by Josh Arnold

Key Metrics

Current Price:	\$43	5 Year CAGR Estimate:	12.3%	Market Cap:	\$35 B
Fair Value Price:	\$51	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	07/22/22
% Fair Value:	84%	5 Year Valuation Multiple Estimate:	3.5%	Dividend Payment Date:	08/05/22
Dividend Yield:	3.4%	5 Year Price Target	\$68	Years Of Dividend Growth:	12
Dividend Risk Score:	C	Retirement Suitability Score:	C	Rating:	Buy

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 more than \$16 billion in annual revenue and a market capitalization of \$35 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 released second quarter earnings on July 15th, 2022, and results were mixed. Earnings-per-share missed estimates by nine cents, coming to \$1.03. Revenue, however, was quite strong at \$4.3 billion, up almost 9% year-over-year, and \$130 million ahead of expectations. The CEO noted that client activity was strong, but that earnings were crimped by lower market values.

Fee revenue was \$3.38 billion, up from \$3.2 billion in Q1, and \$3.2 billion in the year-ago period. This reflected lower money market fee waivers, higher client activity, and higher forex revenue. This was partially offset by the stronger dollar, and lower market values.

Assets under custody declined 4% to \$43 trillion, which was partially offset by client inflows and net new business. The decline was due to market depreciation and a strengthening dollar. Assets under management fell 17% to \$1.9 trillion in Q2.

Provisions for credit losses were \$47 million, down from a benefit of \$86 million, reflecting adverse changes in the economic forecast. We've reduced our estimate of earnings-per-share to \$4.25 following Q2 results. The company also boosted its dividend for the 12th consecutive year.

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	\$4.25	\$5.69
DPS	\$0.52	\$0.58	\$0.66	\$0.68	\$0.72	\$0.86	\$1.04	\$1.18	\$1.24	\$1.33	\$1.48	\$1.89
Shares¹	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 6% earnings-per-share growth annually moving forward.

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

¹ Share count in millions

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also see the bank continuing its share repurchases over time, resulting in a meaningful tailwind for earnings-per-share outside of revenue and 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	10.1	12.0
Avg. Yld.	2.3%	1.9%	1.8%	1.6%	1.8%	1.7%	2.0%	2.5%	3.2%	2.6%	3.4%	2.8%

The stock's earnings multiple is now just 10.1, 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 to return to sub-3% in the coming years.

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%	35%	33%

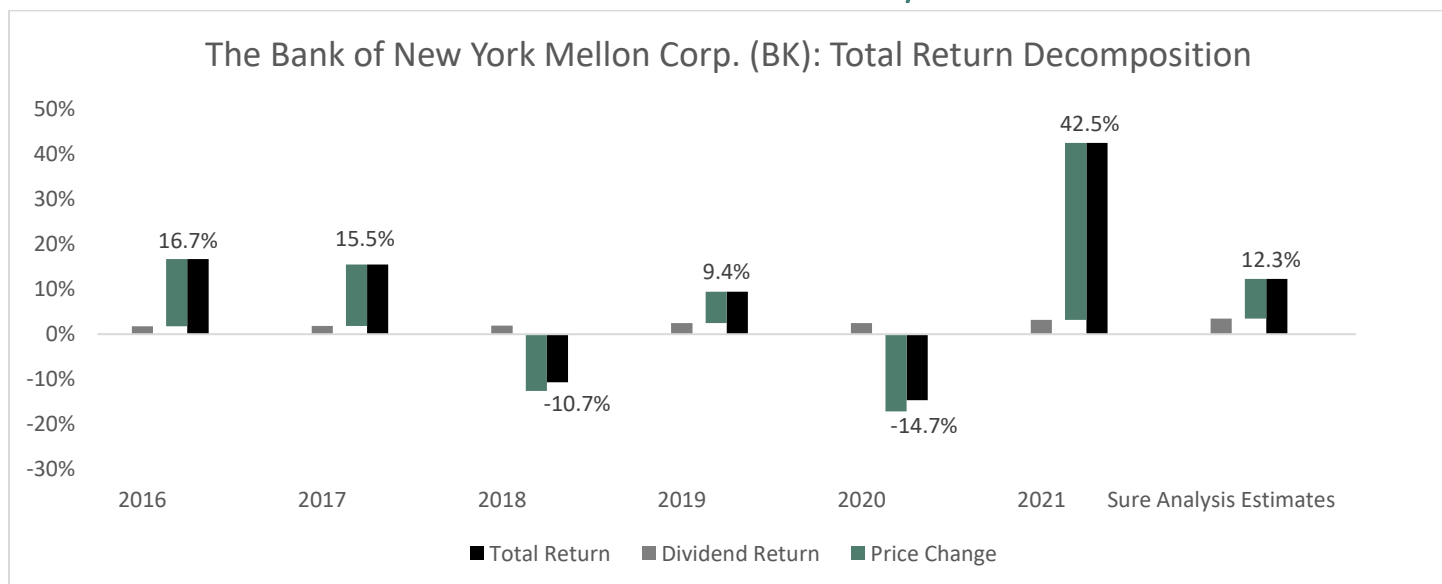
BNY Mellon's dividend is only about a third of its earnings, consistent with other large bank peers. That means the payout is very safe and we expect it to continue growing in the mid-single digits annually in the years to come.

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 decent growth potential. We are forecasting total annual returns of 12.3% going forward, given the valuation, 3.4% yield, and moderate earnings growth from what should be a relatively low base for 2022. We are upgrading the stock from hold to buy after Q2 results.

Total Return Breakdown by Year



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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.

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