State Street Corp. (STT)

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Key Metrics

Current Price:	$66	**5 Year CAGR Estimate:**	18.0%	**Market Cap:**	$22.0 B
Fair Value Price:	$98	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	9/29/22[1]
% Fair Value:	68%	**5 Year Valuation Multiple Estimate:**	8.1%	**Dividend Payment Date:**	10/11/22
Dividend Yield:	3.5%	**5 Year Price Target**	$137	**Years Of Dividend Growth:**	12
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Rating:**	Buy

Overview & Current Events

State Street Corporation is a Boston based financial services company which traces its roots back to 1792. It trades under the ticker STT and has raised its dividend for 12 consecutive years. State Street is one of the largest asset management firms in the world, with approximately $4 trillion of assets under management and $41 trillion of assets under custody and administration. The company trades with a $22 billion market capitalization.

In September of 2021, State Street announced the acquisition of Brown Brothers Harriman Investor Services for $3.5 billion, which rendered State Street the number one asset servicing firm globally. Asset servicing provides back-end operations for many of the world's most popular funds and ETF's. State Street's main competitors include BlackRock, Bank of New York Mellon, and Vanguard.

In mid-July, State Street reported (7/15/22) financial results for the second quarter of fiscal 2022. Fee revenues dipped -6% over last year's quarter due to headwinds from weaker stock markets and bond markets. However, net interest income grew 25% thanks to higher interest rates and the bank generated high forex trading earnings and kept its total expenses essentially flat. As a result, its earnings-per-share grew 11% sequentially, from $1.57 to $1.74, and exceeded the analysts' consensus by $0.20. The stock rallied 10% after its earnings release. Despite the impressive results, we have kept our forecast for the annual earnings-per-share intact due to the unpredictable forex performance of the bank.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$4.20	$4.43	$4.53	$4.77	$5.40	$5.67	$6.89	$6.00	$6.78	$7.52	***$7.80***	***$10.94***
DPS	$0.96	$1.04	$1.16	$1.32	$1.44	$1.60	$1.78	$1.98	$2.08	$2.18	***$2.28***	***$3.28***
Shares[2]	481	455	432	414	396	380	376	374	357	358	***350***	***315***

Over the past 10 years, State Street has grown its dividend at an average annual rate of 11.7%. Going forward, we see the ability for continued growth thanks to the organic growth of equity flows, acquisitions, and the relatively conservative payout ratio of the firm. We consider this a defensive, low-risk stock, which is appropriate for those looking for stable dividend income that can grow faster than inflation in the upcoming years.

In the past few years, State Street has benefitted from new equity inflows as well as a market rally. The bank's asset management business, State Street Global Advisors, also benefitted from stock market gains and flows into ETFs. The firm will rely on the growth of flows into the equity market as well as acquisitions. Management claims to need about $1.5 trillion in new business annually to stick to growth targets.

We are forecasting growth of earnings-per-share of 7% per year over the next five years. State Street has announced the repurchase of $3.0 billion of shares until the end of 2023. This amount represents 12% of the current share count. Organic earnings growth has been about 2.9% per year, while the share count has contracted by more than -3% per year over the last decade. Organic growth, share repurchases and inorganic growth through strategic acquisitions provide the basis of our earnings-per-share growth estimate.

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[1] Estimated date.

[2] In millions.

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Avg. P/E	10.3	14.0	15.4	16.6	12.9	14.7	14.1	11.2	10.4	11.3	***8.5***	***12.5***
Avg. Yld.	2.2%	1.6%	1.6%	1.8%	2.2%	1.8%	2.0%	3.1%	3.2%	2.6%	***3.5%***	***2.4%***

State Street is currently trading at a 10-year low price-to-earnings ratio of 8.5, which is much lower than its 10-year average of 13.1. The cheap valuation has resulted from the surge of inflation to a 40-year high and fears of an upcoming recession. We view these headwinds as temporary and assume a fair price-to-earnings ratio of 12.5 for this stock. If the stock trades at its fair valuation level in five years, it will enjoy an 8.1% annualized valuation tailwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

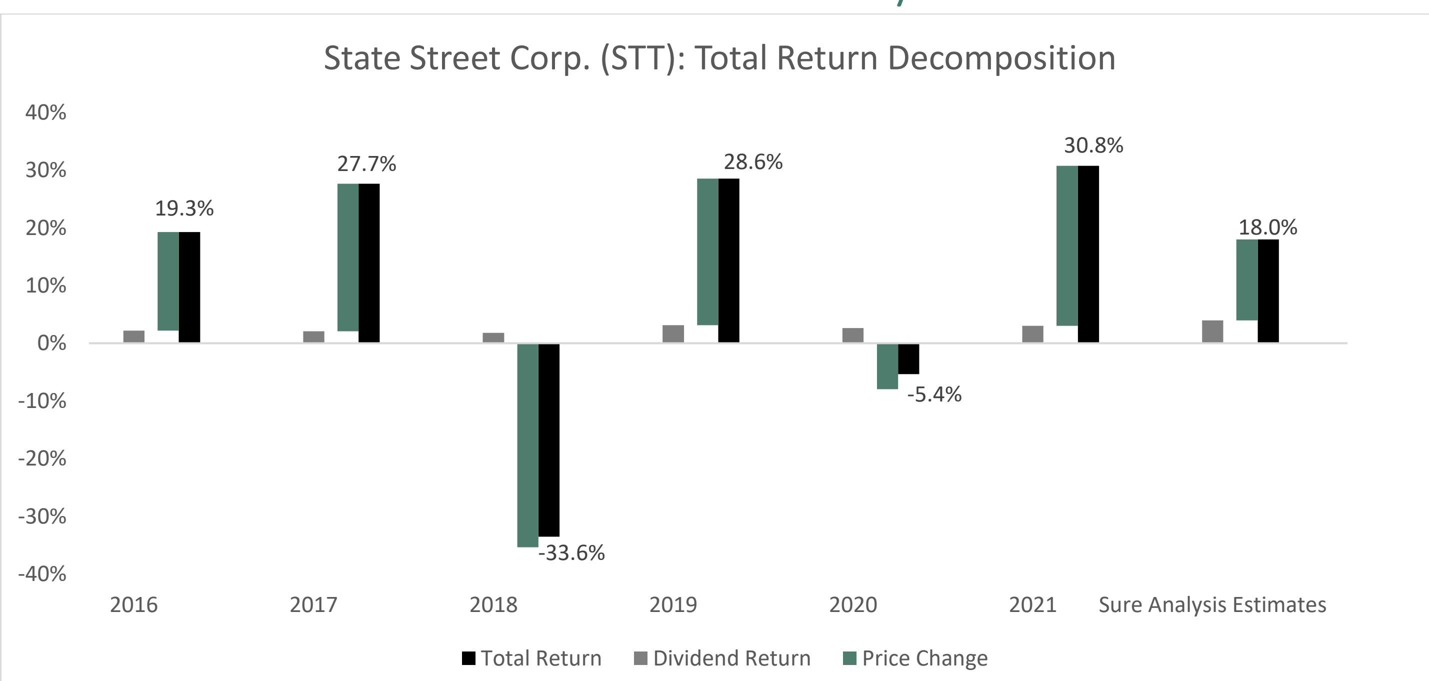
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	23%	23%	26%	28%	27%	28%	26%	33%	31%	29%	***29%***	***30%***

State Street has a conservative payout ratio of 29%, with stable earnings and a solid track record. It is one of the market leaders in its industry of asset management and asset servicing. It also benefits from its economies of scale, which pose a formidable barrier to new entrants. However, competition with names like Vanguard, BlackRock, and Bank of New York Mellon, all of which are lowering fees to attract investor funds, limits the growth potential within this space. A recessionary environment may lower profits but would not necessarily endanger the dividend or the firm.

Final Thoughts & Recommendation

The stock of State Street has shed -30% this year, more than the broad stock market, due to fears that the aggressive interest rate hikes of the Fed in response to 40-year high inflation will cause a recession. We view these headwinds as temporary and view the stock as exceptionally attractive from a long-term point of view. State Street could offer an 18.0% average annual return over the next five years thanks to 7% earnings-per-share growth, a 3.5% starting dividend yield and the potential for an 8.1% annualized valuation tailwind. The stock earns a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	8,947	9,079	9,422	9,567	9,407	10,418	11,094	10,698	10,684	11,003
SG&A Exp.	3,837	3,880	4,140	4,357	4,560	4,561	4,983	4,717	4,559	4,554
D&A Exp.	489	675	699	801	929	1,085	1,203	1,337	1,510	---
Net Profit	2,061	2,050	2,022	1,980	2,143	2,156	2,593	2,242	2,420	2,693
Net Margin	23.0%	22.6%	21.5%	20.7%	22.8%	20.7%	23.4%	21.0%	22.7%	24.5%
Free Cash Flow	1,578	-2,412	-988	-2,106	1,677	6,303	9,566	4,960	2,972	---
Income Tax	705	616	415	318	-22	839	508	470	479	478

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets ($B)	222.6	243.3	274.1	245.2	242.7	238.4	244.6	245.6	314.7	314.6
Cash & Equivalents	53,527	67,654	95,575	76,672	72,381	69,454	76,310	72,325	120,485	109,989
Acc. Receivable	2,481	3,073	2,755	3,364	3,530	3,447	3,511	3,663	3,484	3,278
Goodwill & Int.	8,516	8,396	7,851	7,439	7,564	7,635	9,815	9,586	9,510	9,437
Total Liab ($B)	201.7	222.9	252.8	224.0	221.5	216.1	219.9	221.2	288.5	287.3
Long-Term Debt	11,225	12,691	13,654	12,917	12,722	12,514	13,995	13,212	17,689	13,603
Total Equity	20,380	19,887	19,367	18,400	18,023	19,121	21,047	21,469	23,729	25,387
D/E Ratio	0.54	0.62	0.64	0.61	0.60	0.56	0.57	0.54	0.68	0.50

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	0.9%	0.9%	0.8%	0.8%	0.9%	0.9%	1.1%	0.9%	0.9%	0.9%
Return on Equity	10.5%	10.2%	10.3%	10.5%	11.8%	11.6%	12.9%	10.5%	10.7%	11.0%
ROIC	6.5%	6.3%	5.9%	5.7%	6.3%	6.3%	7.0%	5.9%	5.9%	6.3%
Shares Out.	481	455	432	414	396	380	376	374	357	358
Revenue/Share	18.60	19.95	21.81	23.13	23.75	27.40	29.47	28.63	29.92	30.74
FCF/Share	3.28	-5.30	-2.29	-5.09	4.23	16.58	25.41	13.27	8.32	---

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