Financial Institutions, Inc. (FISI)

Updated September 25th, 2023, by Yiannis Zourmpanos

Key Metrics

Current Price:	$17	**5 Year CAGR Estimate:**	12.0%	**Market Cap:**	$265.8 M
Fair Value Price:	$16	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	12/13/2023[1]
% Fair Value:	104%	**5 Year Valuation Multiple Estimate:**	-0.7%	**Dividend Payment Date:**	12/28/2023
Dividend Yield:	7.1%	**5 Year Price Target**	$23	**Years Of Dividend Growth:**	13
Dividend Risk Score:	C	**Retirement Suitability Score:**	B	**Rating:**	Buy

Overview & Current Events

Financial Institutions is a chartered institution serving New York individuals, municipalities, and businesses. Its offerings include diverse checking and savings accounts, like money market options, certificates of deposit, and individual retirement and NOW accounts. They extend various loans, encompassing term loans, credit lines, commercial loans for capital needs, business expansion, equipment purchase, agricultural and residential mortgages, home equity loans, and consumer loans. The company also delivers personal and commercial insurance solutions, from auto and homeowners to worker's compensation, bonds, and more. Additionally, they offer financial services such as life insurance, annuities, and retirement plans.

On July 27th, 2023, the company announced results for the second quarter of 2023. Financial Institutions reported Q2 Non-GAAP EPS of $0.91, beating estimates by $0.16. The company reported revenues of $53 million for the quarter, up 16.8% year-over-year. Net interest income reached $42.3 million, increasing 1.2% from the previous quarter and 1.8% from the same period last year due to rising interest rates and associated yields and costs. The company successfully merged its two SEC-registered investment advisory firm subsidiaries. HNP Capital, LLC merged into Courier Capital, LLC, creating one of Western New York's largest registered investment advisory firms with $2.75 billion in assets under management as of June 30th, 2023.

Financial Institutions' recent financials show favorable loan growth, particularly in commercial mortgages, indicating a strong lending portfolio. However, declining investment securities and public deposits could limit income diversity and liquidity. The impact of rising interest rates on the securities portfolio has adversely affected shareholders' equity and book value per share. While the dividend increase, and regulatory solid capital ratios signal financial stability, concerns remain about asset quality and risk management, especially given the volatility in interest rates. To maintain sustainable growth, FISI must focus on managing its securities portfolio effectively and maintaining the quality of its loan portfolio. It is adjusting its 2023 loan growth outlook from high single-digit to low double-digit growth, indicating confidence in early-year lending prospects.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$1.75	$2.00	$1.90	$2.10	$2.13	$2.39	$2.96	$2.30	$4.78	$3.56	***$3.26***	***$4.57***
DPS	$0.74	$0.77	$0.80	$0.81	$0.85	$0.96	$1.00	$1.04	$1.08	$1.16	***$1.20***	***$1.53***
Shares	13.8	13.9	14.1	14.5	15.1	16.0	16.0	16.1	15.9	15.5	***15.7***	***16.8***

Financial Institutions has reported mixed performance lately. On the positive side, net interest income increased slightly compared to the previous quarter and the same period in the previous year, reaching $42.3 million. However, this growth was driven by an expansion in average interest-earning assets, primarily due to increased loans and cash holdings, offset by reduced investment securities. The concerning aspect is the decline in the net interest margin, which dropped to 2.99% from 3.09% in the first quarter of 2023 and 3.19% in the second quarter of 2022. This decline can be attributed to a change in deposit composition, with more customers opting for higher-cost time deposits amidst rising

[1] Estimated ex-dividend date

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.

Financial Institutions, Inc. (FISI)

Updated September 25th, 2023, by Yiannis Zourmpanos

interest rates. Additionally, seasonality and repricing in the public deposit portfolio contributed to this margin compression. In line with the company's guidance and high-interest rate environment for Financial Institutions, we expect the company to post EPS of $3.26 in 2023. We maintain our EPS growth forecast of 7.0% over the next five years, leading to our estimated EPS of $4.57 by 2028. Moreover, the company has a solid record of paying dividends despite operating in a dynamic macro environment, as Financial Institutions have paid increasing dividends for the past 13 years. We expect the company to maintain its dividend growth and have forecasted a compound annual dividend growth rate of 5.0%, leading to a dividend of $1.53 in 2028.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Avg. P/E	11.9	11.6	12.9	13.4	14.7	12.8	10.0	8.7	6.3	7.6	***5.2***	***5.0***
Avg. Yld.	6.6%	5.6%	4.9%	4.5%	5.3%	6.3%	5.6%	6.4%	5.6%	7.8%	***7.1%***	***6.7%***

The regional bank trades at a forward P/E of 5.2, considerably lower than the long-term average P/E of 11.0 and the five-year average P/E of 9.1. Even though the high-interest rate environment and the merger will benefit the company in the near term, we assign a P/E multiple of 5.0 to the stock, which is a fair reflection of its value. Accordingly, with expected EPS of $4.57 and P/E of 5.0, our target price for the stock stands at $23 by 2028.

Safety, Quality, Competitive Advantage, & Recession Resiliency

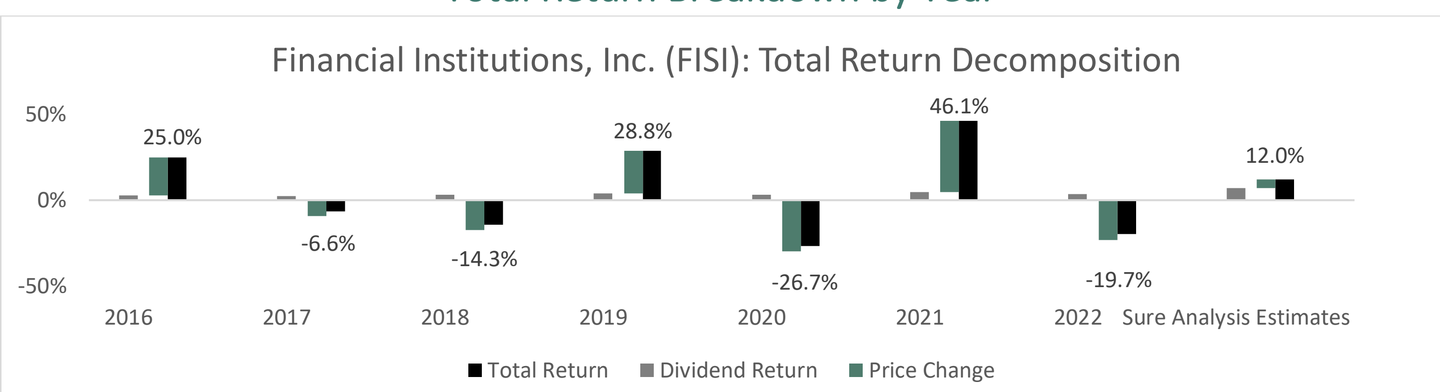
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	42%	39%	42%	39%	40%	40%	34%	45%	23%	33%	***37%***	***36%***

The company has paid a consistent dividend to its shareholders with a 10-year payout ratio averaging 37.6%, and we expect the company to maintain and increase its payout in the future. Financial Institutions initiated a share repurchase program in June 2022, authorizing the repurchase of up to 766,447 shares of common stock. As of June 30th, 2023, there were 766,447 shares still available for repurchase under this program. Financial Institution's cash and cash equivalents increased by $49.8 million from December 31st, 2022, to June 30th, 2023, reaching $180.2 million.

Final Thoughts & Recommendation

While Financial Institutions runs a regional banking business, we believe that increased benchmark rates and the merger will be the positive catalysts for EPS growth. Indeed, Financial Institutions' dividend growth prospects remain strong throughout the long term under multiple economic uncertainties. Hence, the buy rating is premised upon 12.0% annualized expected total returns for the medium-term, derived from the forecasted earnings-per-share growth of 7.0%, the 7.1% dividend yield, and a tailwind based on the Fed's quantitative tightening.

Total Return Breakdown by Year



Click here to rate and review this research report. Your feedback is important to us.

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.

Financial Institutions, Inc. (FISI)

Updated September 25th, 2023, by Yiannis Zourmpanos

Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	116	120	125	138	147	158	170	182	200	212
SG&A Exp.	45	46	53	56	60	72	73	66	67	76
D&A Exp.	4	5	5	6	6	6	8	8	8	8
Net Profit	26	29	28	32	34	40	49	38	78	57
Net Margin	22.1%	24.4%	22.6%	23.1%	22.8%	25.0%	28.8%	21.1%	38.9%	26.6%
Free Cash Flow	34	30	36	39	39	62	54	39	64	125
Income Tax	12	10	11	12	10	10	11	7	20	14

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	2,929	3,090	3,381	3,710	4,105	4,312	4,384	4,912	5,521	5,797
Cash & Equivalents	60	58	60	71	99	103	113	94	79	130
Goodwill & Int.	50	69	67	76	75	76	75	74	74	73
Total Liabilities	2,674	2,810	3,087	3,390	3,724	3,915	3,945	4,444	5,016	5,392
Long-Term Debt	298	295	332	371	485	509	315	79	104	279
Total Equity	237	262	277	303	364	379	422	451	488	388
D/E Ratio	1.17	1.06	1.13	1.16	1.27	1.28	0.72	0.17	0.21	0.69

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	0.9%	1.0%	0.9%	0.9%	0.9%	0.9%	1.1%	0.8%	1.5%	1.0%
Return on Equity	10.8%	11.7%	10.5%	11.0%	10.1%	10.6%	12.2%	8.8%	16.6%	12.9%
ROIC	5.4%	5.2%	4.7%	4.9%	4.3%	4.5%	5.9%	5.9%	13.4%	8.7%
Shares Out.	13.8	13.9	14.1	14.5	15.1	16.0	16.0	16.1	15.9	15.5
Revenue/Share	8.38	8.63	8.85	9.53	9.76	9.91	10.60	11.33	12.52	13.73
FCF/Share	2.45	2.14	2.52	2.70	2.55	3.90	3.37	2.44	3.99	8.09

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