Unity Bancorp, Inc. (UNTY)

Published September 4th, 2024, by Kody Kester

Key Metrics

Current Price:	$34	**5 Year CAGR Estimate:**	10.5%	**Market Cap:**	$336M
Fair Value Price:	$38	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	09/06/24
% Fair Value:	90%	**5 Year Valuation Multiple Estimate:**	2.1%	**Dividend Payment Date:**	09/20/24
Dividend Yield:	1.5%	**5 Year Price Target**	$53	**Years Of Dividend Growth:**	11
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Buy

Overview & Current Events

Founded in 1991 under the name First Community Bank, Unity Bancorp, Inc. is a community bank. UNTY serves as the holding company of Unity Bank.

The company is a full-service commercial bank that mostly serves businesses and consumers in Bergen, Hunterdon, Middlesex, Morris, Ocean, Somerset, Union, and Warren counties in New Jersey. To a lesser extent, Unity Bank reaches into the New York City metropolitan area and Northampton County in Pennsylvania with its banking locations and online services. As of June 30, UNTY had $2.6 billion in assets.

The bank's savings products offered to customers include personal and business checking accounts, savings accounts, and money market accounts. UNTY also provides Small Business Administration loans, commercial loans, mortgage loans, home equity loans, and personal loans. Additionally, the company offers debit and credit cards, safe deposit boxes, and internet and mobile banking services.

Among banks with less than $5 billion in assets, Bank Director ranks UNTY as the 13th best in the nation. The company's commitment to meeting the needs of customers earned it this distinction. Not to mention that UNTY's efficiency placed it fifth among all banks under $5 billion in assets for return on assets at around 1.6%.

On July 12th, the community bank shared its financial results for the second quarter ended June 30. UNTY's net interest income decreased by 0.4% year-over-year to $23.4 million during the quarter. Higher interest income was canceled out by more interest paid on deposits to remain competitive versus other banks. This resulted in a 3-basis point contraction in net interest margin to 4.01% in the quarter. UNTY's diluted EPS fell by 2.1% over the year-ago period to $0.93 for the quarter. This exceeded the analyst consensus by $0.02 during the quarter.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$0.81	$1.12	$1.38	$1.20	$2.01	$2.14	$2.19	$3.43	$3.59	$3.84	***$3.78***	***$5.30***
DPS	$0.09	$0.13	$0.17	$0.23	$0.27	$0.31	$0.32	$0.36	$0.43	$0.48	***$0.52***	***$0.73***
Shares[1]	8.4	9.3	10.5	10.6	10.8	10.9	10.5	10.4	10.6	10.1	***10.0***	***9.5***

In the past decade, UNTY's diluted EPS has nearly quintupled. Now that the bank is working with a bigger earnings base, this probably won't be replicated in the coming years. However, we do believe that diluted EPS growth can still be in the high-single-digits annually over the medium term. This is because later this month, the first of a series of interest rate cuts are anticipated from the Federal Reserve. That should help stimulate borrowing activity and disincentivize saving again. This tends to push net interest margins higher for banks, which will aid UNTY's diluted EPS growth.

In recent years, the company's share count has gradually moved lower over time. We expect this to continue in the years to come, which is why we are projecting a 5% lower share count by 2029.

[1] Share count is 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.

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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Avg. P/E	10.5	10.1	11.4	16.5	10.0	10.3	8.0	7.7	7.6	7.7	***9.0***	***10.0***
Avg. Yld.	1.1%	1.1%	1.1%	1.2%	1.3%	1.4%	1.8%	1.4%	1.6%	1.6%	***1.5%***	***1.4%***

In the past 10 years, UNTY's P/E ratio has varied from as low as the high-single-digits to the mid-teens. This explains the average P/E ratio of 10 in that time. Because the company's growth prospects appear to be intact and it is one of the best community banks in the country, we believe that a return to a P/E ratio of 10 is a conservative assumption. Relative to the current P/E ratio of 9, this could make UNTY an interesting value right now.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	11%	12%	12%	19%	13%	14%	15%	10%	12%	13%	***14%***	***14%***

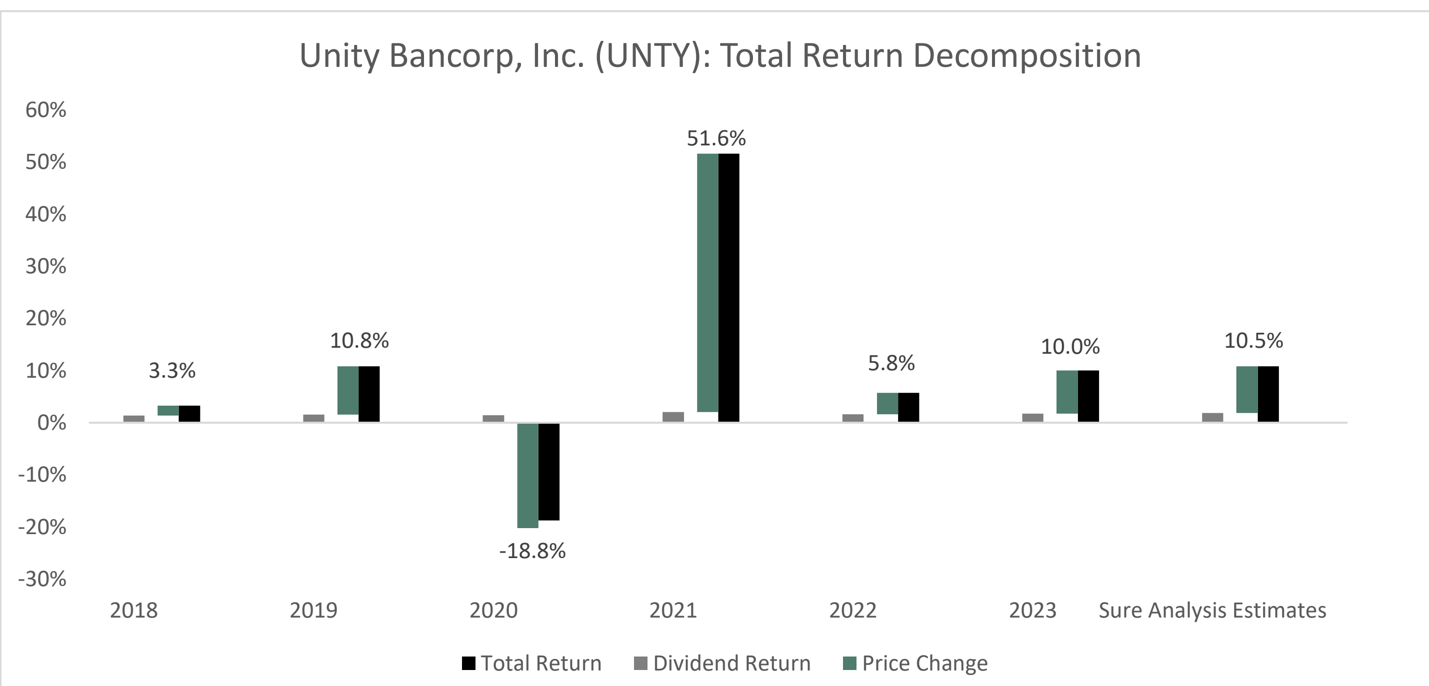
UNTY has managed to achieve a lot in its 33-year operating history. As one of the leading banks headquartered in New Jersey, the company blends the feel of a bigger bank with the hometown charm of a smaller bank. This keeps existing customer retention elevated and attracts new customers as well.

The company's asset quality is reasonably strong, too. As of June 30, the company's nonperforming assets ratio was 0.33%. UNTY's dividend payout ratio is another positive. As it has for most of the past 10 years, this is set to remain in the low teens in 2024. That provides a significant buffer for the company to extend its 11-year dividend growth streak with dividend growth at least matching diluted EPS growth in the years ahead.

Final Thoughts & Recommendation

UNTY's 1.5% dividend yield, 7.0% annual diluted EPS growth potential, and 2.1% annual valuation multiple expansion could generate 10.5% annual total returns in the coming five years. That return potential is decent enough to justify initiating coverage with a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	37	42	46	53	63	66	77	88	98	101
SG&A Exp.	16	18	19	21	24	24	25	28	30	33
D&A Exp.	1	1	1	1	2	2	2	2	3	2
Net Profit	6	10	13	13	22	24	24	36	38	40
Net Margin	17.4%	22.9%	28.6%	24.1%	34.8%	35.8%	30.9%	41.0%	39.4%	39.3%
Free Cash Flow	11	2	(1)	13	37	32	22	31	41	46
Income Tax	3	5	7	10	5	7	7	12	13	13

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	1,009	1,085	1,190	1,455	1,579	1,719	1,959	2,034	2,445	2,579
Cash & Equivalents	29	23	22	24	20	21	23	245	115	195
Accounts Receivable	4	4	4	5	6	7	10	10	13	14
Goodwill & Int. Ass.	2	2	2	2	2	2	2	2	2	2
Total Liabilities	939	1,006	1,084	1,337	1,441	1,558	1,785	1,828	2,206	2,317
Accounts Payable	0	0	0	0	0	0	0	0	1	2
Long-Term Debt	125	92	131	285	220	293	210	50	393	367
Shareholder’s Equity	70	78	106	118	138	161	174	206	239	261
LTD/E Ratio	1.79	1.18	1.24	2.42	1.59	1.83	1.21	0.24	1.64	1.40

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	0.7%	0.9%	1.2%	1.0%	1.4%	1.4%	1.3%	1.8%	1.7%	1.6%
Return on Equity	10.1%	12.9%	14.3%	11.5%	17.1%	15.8%	14.1%	19.0%	17.3%	15.9%
ROIC	3.9%	5.2%	6.5%	4.0%	5.8%	5.8%	5.6%	11.3%	8.7%	6.3%
Shares Out.	8.4	9.3	10.5	10.6	10.8	10.9	10.5	10.4	10.6	10.1
Revenue/Share	4.21	4.45	4.83	4.98	5.77	5.99	7.08	8.35	9.12	9.76
FCF/Share	1.27	0.22	(0.08)	1.20	3.40	2.95	2.01	2.97	3.85	4.45

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