



SunTrust Bank Stock Pitch

NYSE: STI | Target Price - \$84.04 | Current Price - ▲ \$74.15

That Guy With The Glasses

FIN 357

February 27, 2018



1. Company Overview
2. Macroeconomic Outlook
3. Industry Outlook
4. Investment Thesis
5. Valuation
6. Risk Factors
7. Recommendation

Overview of SunTrust, Inc.

Operations:

- SunTrust, Inc. is a super-regional bank holding company that operates in Florida, Georgia, Maryland, North Carolina, South Carolina, Tennessee, Virginia and Washington D.C.
- The company provides financial services such as credit cards, mortgage banking, brokerage, and capital market services

Segments:

- Consumer banking & Private Wealth Management
- Wholesale Banking
- Mortgage Banking

Management



William H. Rogers, Jr.
Chairman and Chief
Executive Office



Jerome T. Lienhard, II
Chief Risk Officer



Laura Allison Dukes
Incoming
Chief Financial Officer



Ernest N. Dawal, Jr.
Chief Investment Officer



General Statistics (2017 Fiscal Year)



– **Sector:** Regional Commercial/Corporate Banking



– **Market Capitalization:** \$ 33.5 Billion



– **Net Interest Income:** \$5,633 million

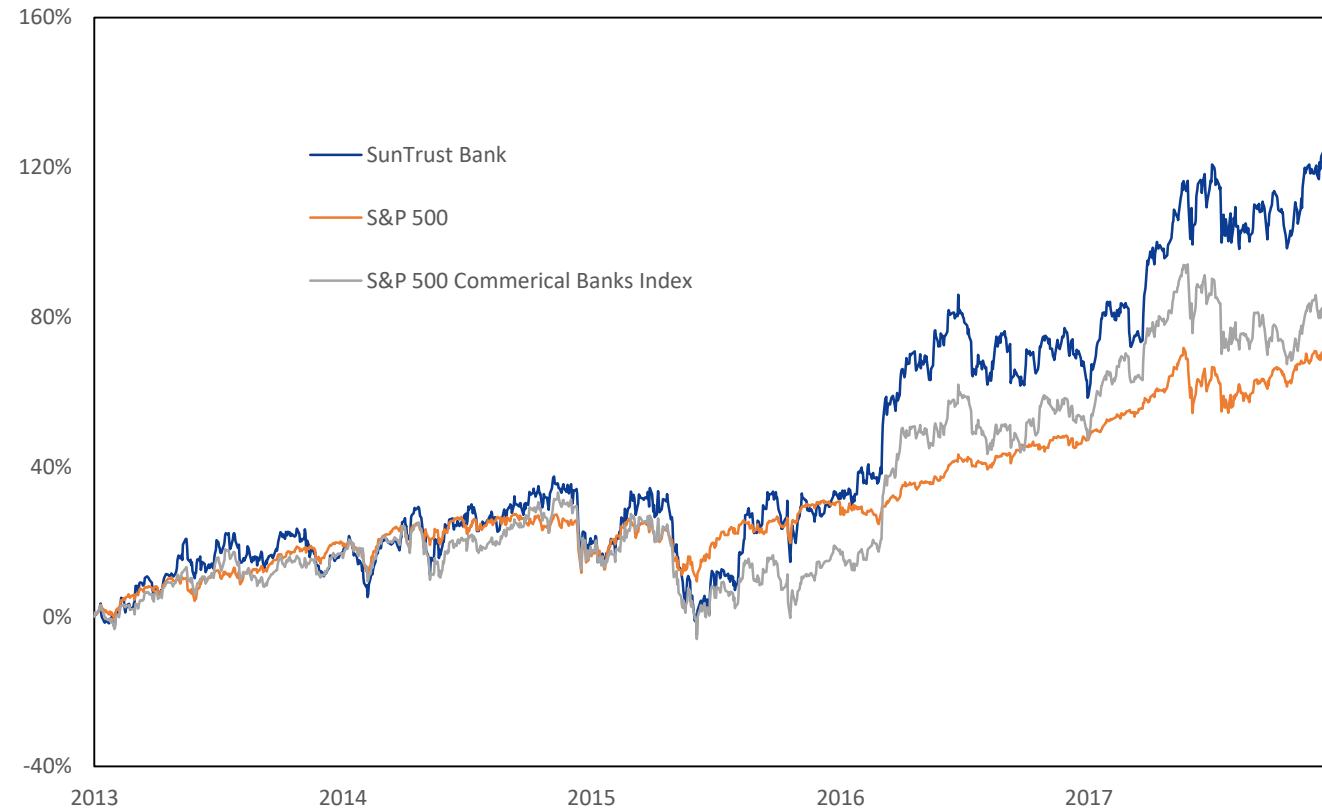


– **Net Income:** \$2,085 million

Company Overview



5-Year Comparative Performance

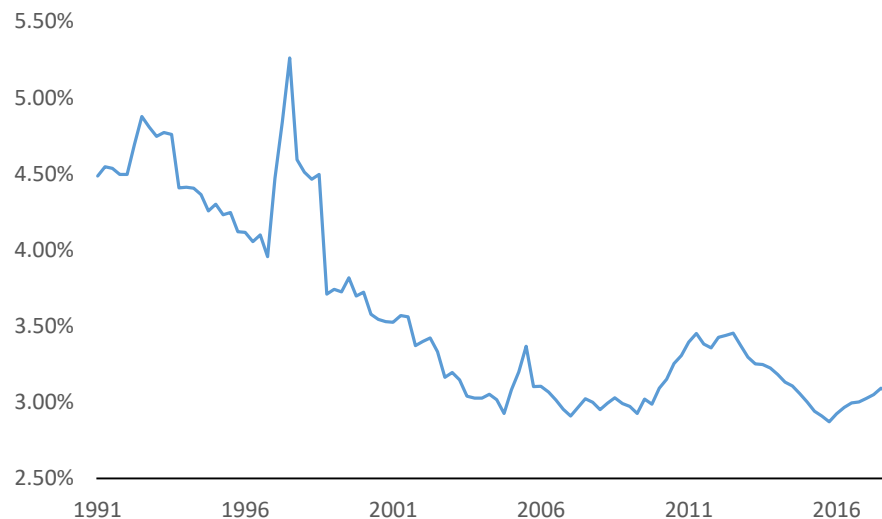


Comparative Return

Company / Index	Price Change	Total Return	Relative	Annual Equivalent Rate
SunTrust Bank	124.88%	150.43%	59.65%	
S&P 500	72.16%	90.78%	-	
S&P 500 Commerical Banks	81.90%	102.62%	11.83%	

Source: Bloomberg

Net Interest Margin



SunTrust Performance (Fiscal Year 2017)

Net Interest Margin:

- Growth %, YoY: 3.06%;

Net Interest Income:

- Growth %, YoY: 23.2%; 5-Year Average: 2.15%

Return on Equity

- Return to Common Shareholders: 9.04% (5-year average: 7.88%)

Loans

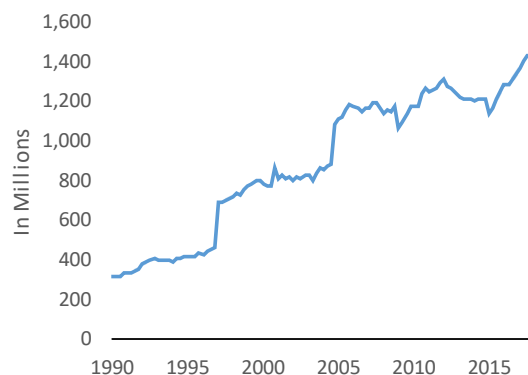
- Total Loans: \$143 billion (-0.63% Growth YoY)

Dividends

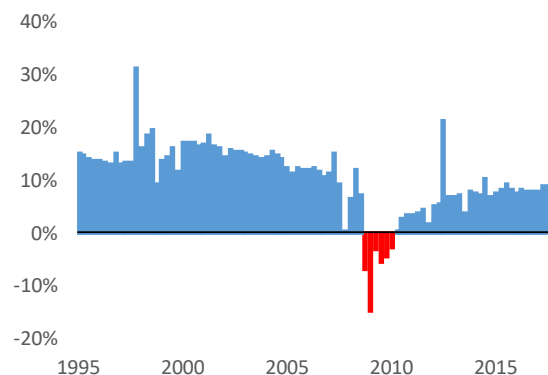
- Growth %, YoY: 27.42%; Payout Ratio: 27.95%

Other Key Performance Metrics

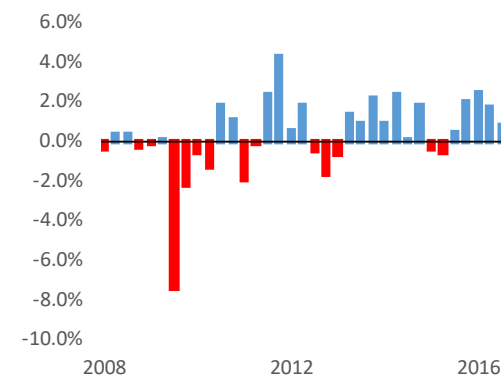
Net Interest Income



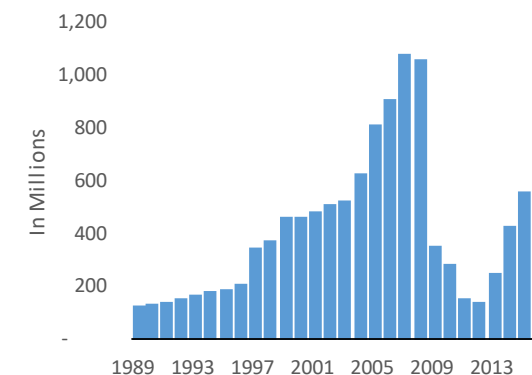
Return on Equity



Total Loans (YoY Growth)

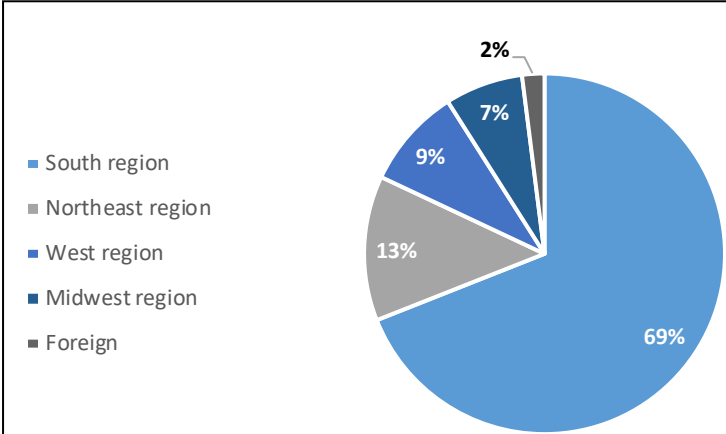


Dividends

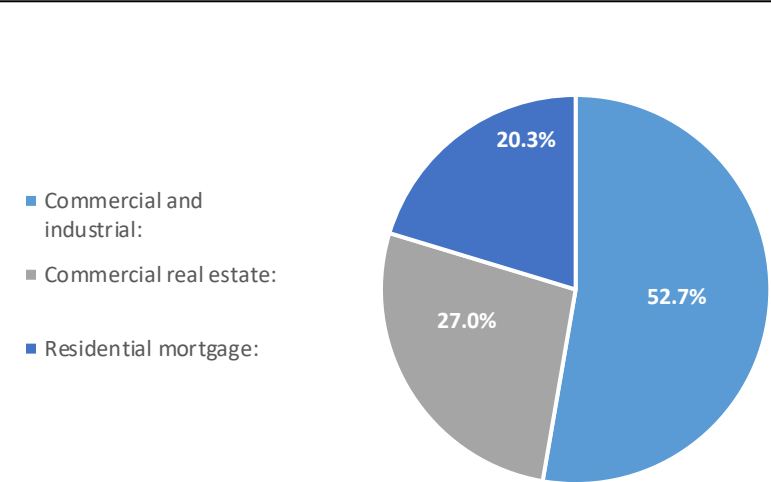


SunTrust Loan Portfolio Mix

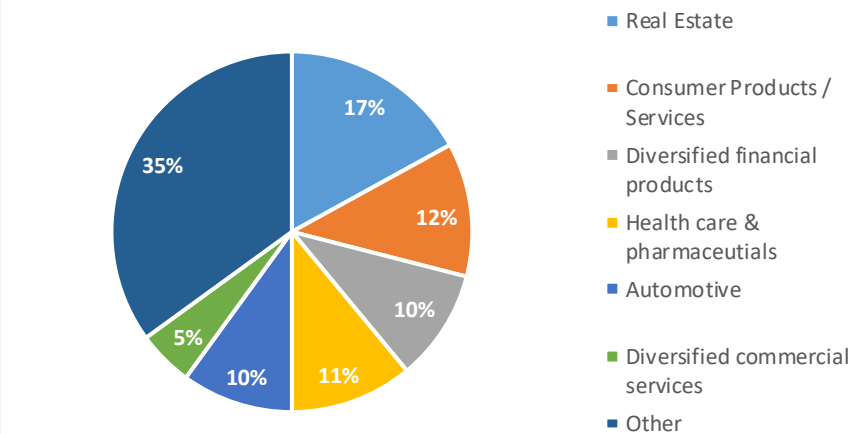
By Region



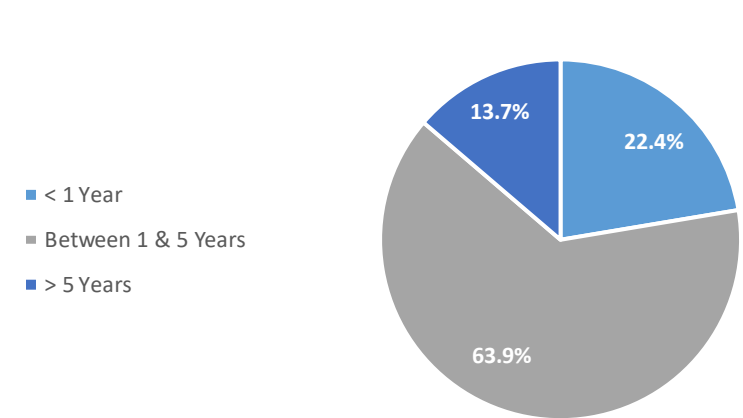
By Type



By Industry



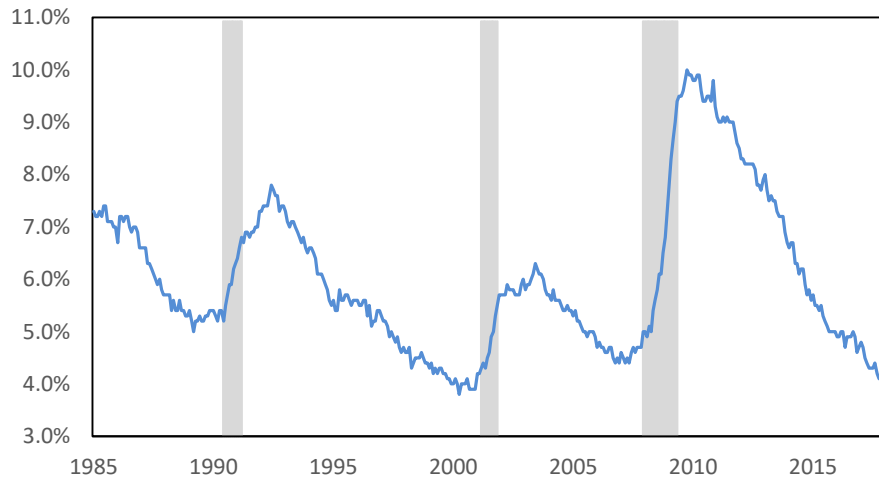
By Duration



Macroeconomic Trends

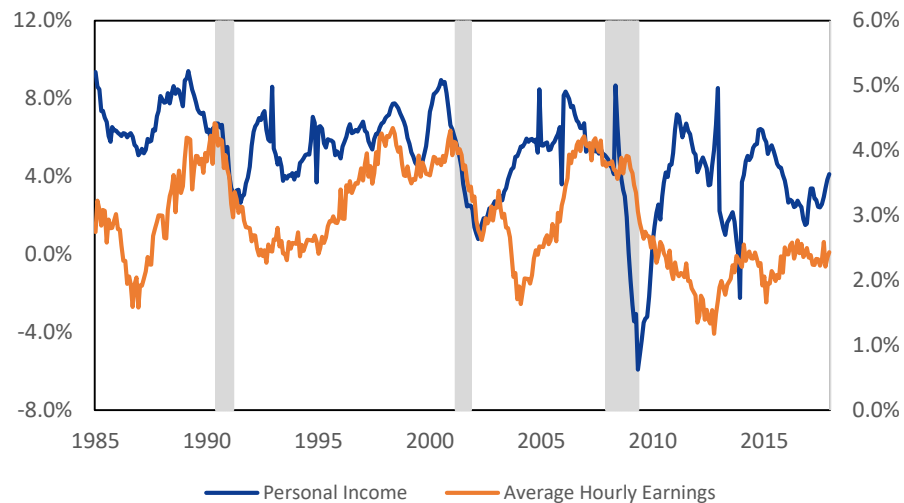


Unemployment Rate



Source: Bureau Labor of Statistics

Personal Income



Source: U.S. Bureau of Economic Analysis; Bureau Labor of Statistics

Improving Labor Market Conditions

- Civilian Unemployment Rate: 4.1%
- 200,000 Thousand Jobs created the month of January; 2,274 thousand for 2017.
- Civilian Labor Force Participation Rate: 62.7%

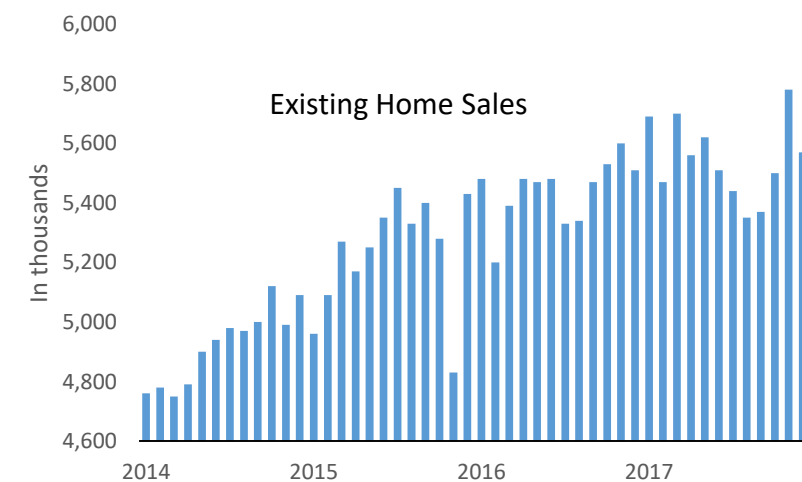
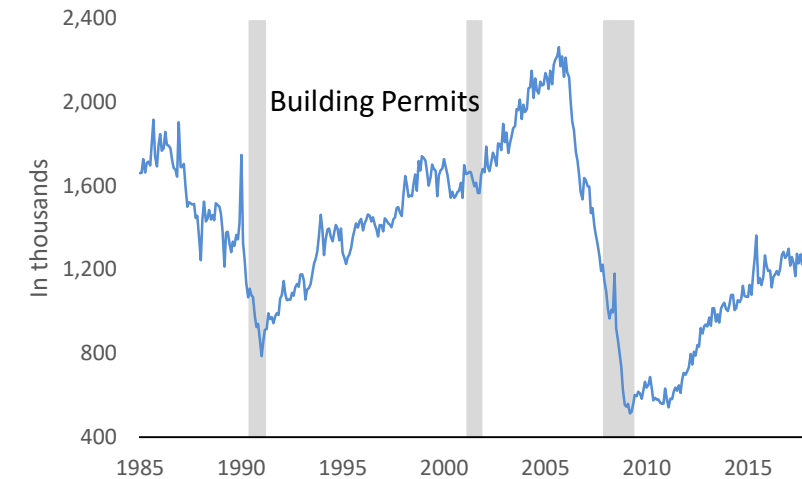
Income & Wage Growth

- Personal Income Growth (YoY): 4.11%
- Average Hourly Earnings (YoY): 2.88%

Housing Market Performance

- Housing market data, as a leading indicator, can be used to gauge future bank profitability
- More existing home sales/building permits can be transformed into higher loan volumes for commercial banks
- Existing home sales increased from 4.7 million in the beginning of 2014 to 5.5 million at the end of 2017
- Building permits increased from an all-time low of 513 thousand in 2010 to 1.3 million in 2017

Housing Market Performance

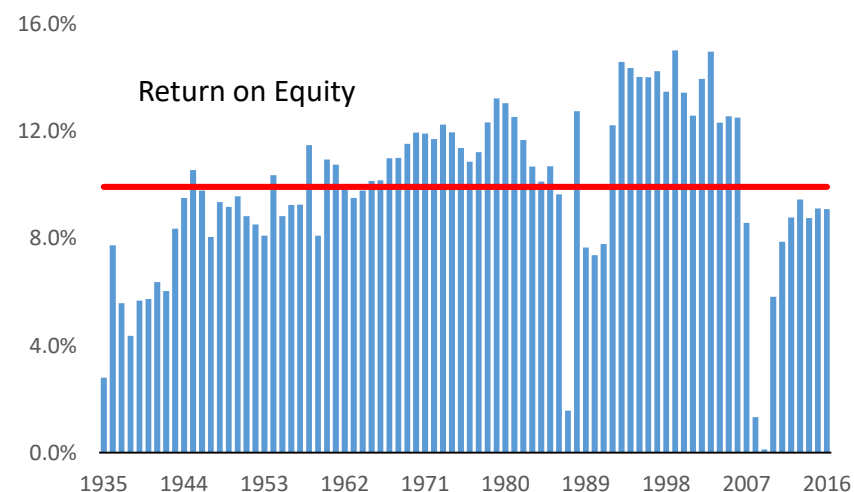
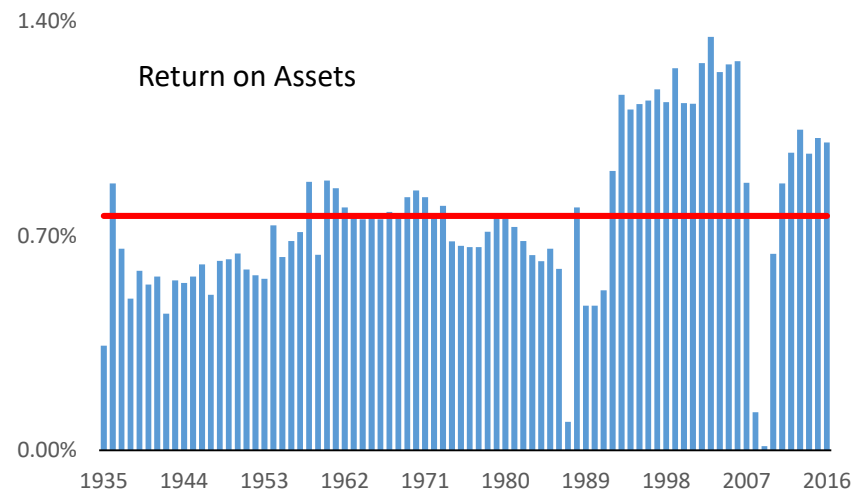


Source: National Association of Realtors

Industry Outlook



Historical Return on Assets & Equity



Source: FDIC

*Data is for all US Commercial Banks

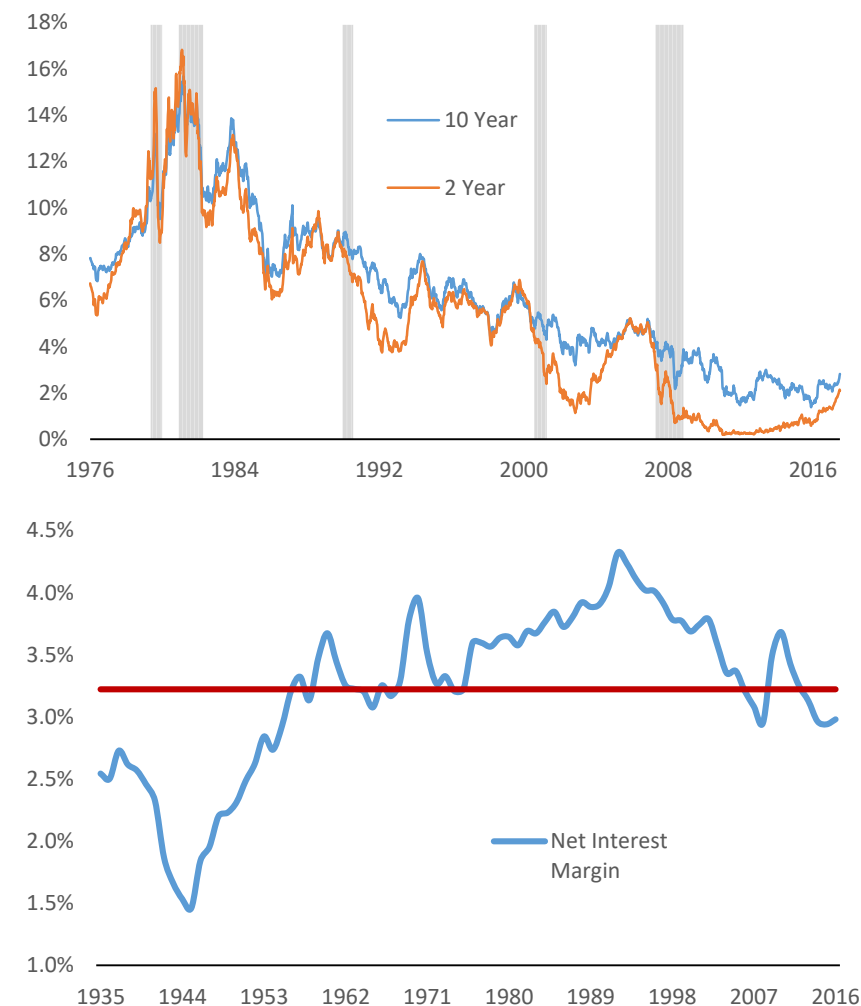
The New Normal

- Macroeconomic trends boosted bank profitability, leading to higher Return on Assets and equity
- Normalized bank returns (ROAs & ROE) should be lower going forward
- Since 1935, banks have traded higher than 1% Return on Assets 17 times in history
- Industry average for Return on Assets is 0.73%
- Industry average for Return on Equity is 9.92%

Deposits are a key driver of Net Interest Income

- Comparing bank deposit rates to market interest rates provide a better sense of how meaningful deposits are to bank profitability
- Deposits provide a stable source of funding and liquidity at a relatively low cost
- Lower rates have placed downward pressure on bank profitability; Higher rates can potentially lead to higher Net Interest Income.
- The spread between the NII and 2-year Treasury yields detail how banks are able to control its funding cost.
- Industry NII / 2-year spread: 0.93%

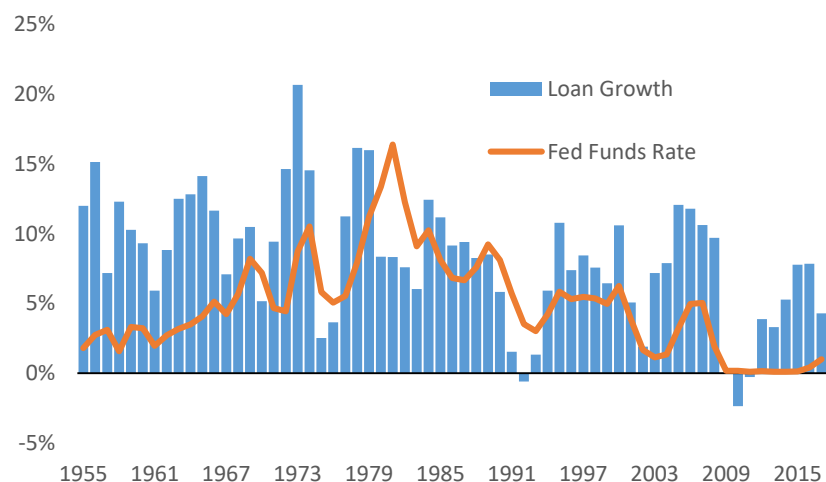
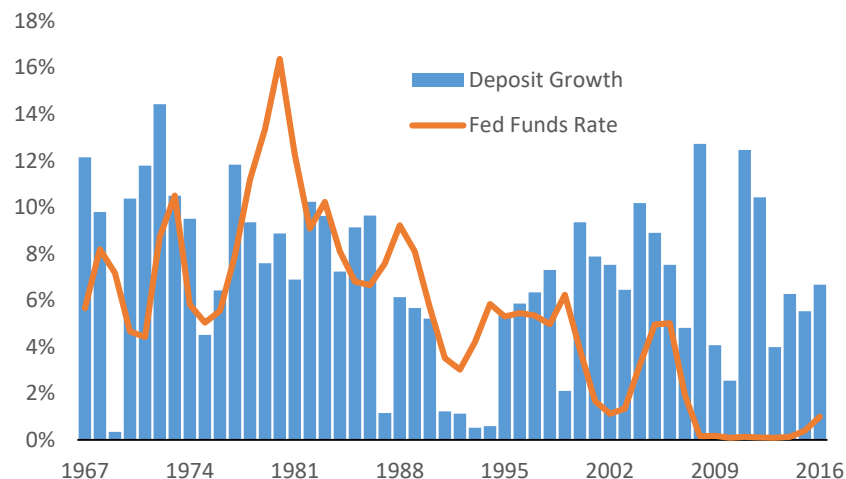
U.S. Treasury Interest Rates (Weekly) & Net Interest Margin



Source: FDIC, Bloomberg

*Data is for all US Commercial Banks

Loan / Deposit Growth vs. Fed Funds Rate



Source: Federal Reserve, FDIC

*Data is for all US Commercial Banks

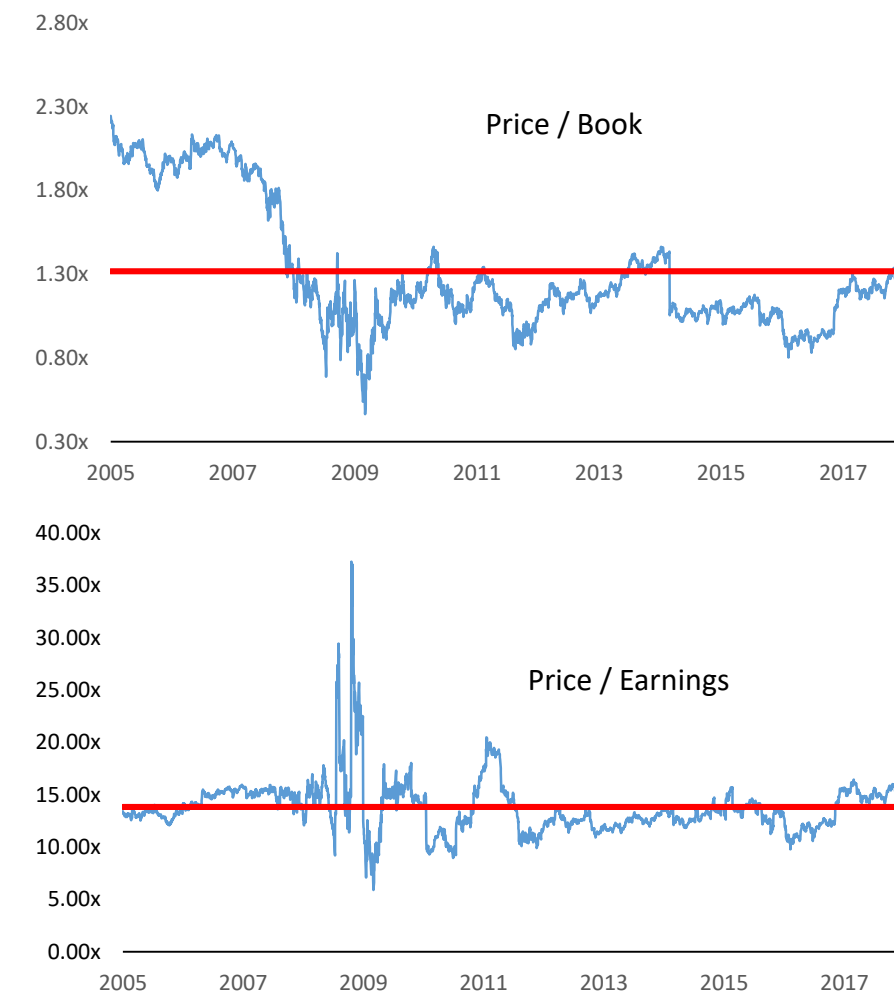
Asset/Liability Sensitivity Management

- Interest rates play an important role in liability management
- Banks with more asset-sensitivity can expect to earn money on interest-earning assets as rates increase
- Banks with more liability-sensitivity can expect to lose money as interest expenses outpace interest income
- As interest rates change, banks need to reprice interest rates on their assets/liabilities, which is challenging.
- As interest rates increase, we can expect an increase in deposits and lower loan volumes.
- How soon and how much a bank reprices its deposits depends on the Banks's strategy, interest rate lags, and other factors

Valuing Commercial Banks

- Banks are valued based on their earnings power, expected growth, and book value
- Book value is especially used during periods of earnings pressure
- More conservative methods, like Price / Tangible Common Book Value, has become widely accepted after the financial crisis
- 12 year average Price / Book 1.32x; 13.83x Price / Earnings
- Current P/B Ratio: 1.55x; Current P/E Ratio: 18.26x

Historical Bank Valuation



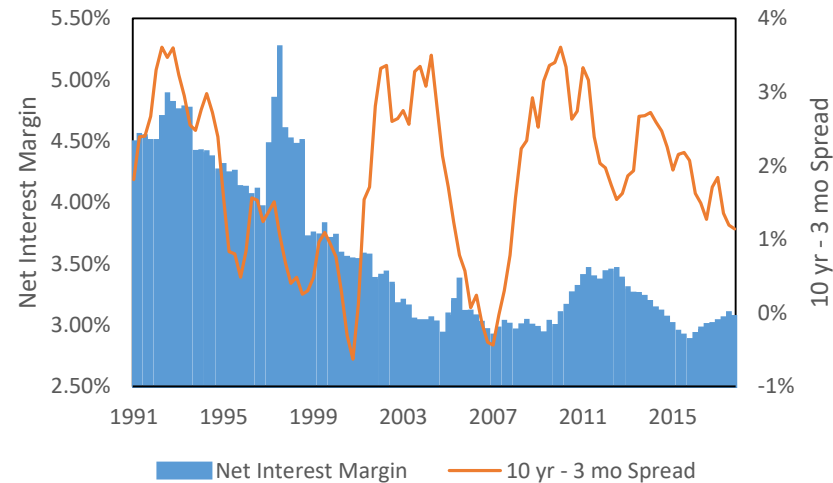
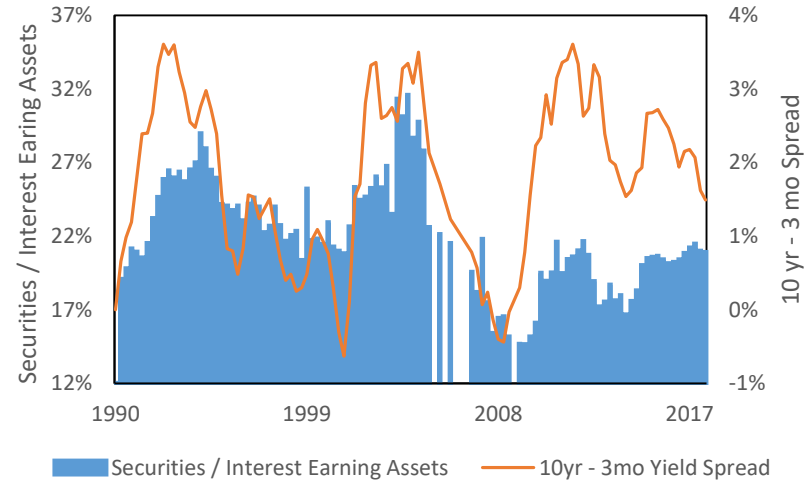
Source: S&P Capital IQ

*Data is for all US Commercial Banks

Investment Thesis



Banking Profitability and Yield Curve Assumptions



Source: Federal Reserve, Bloomberg LP, SunTrust Company Filings

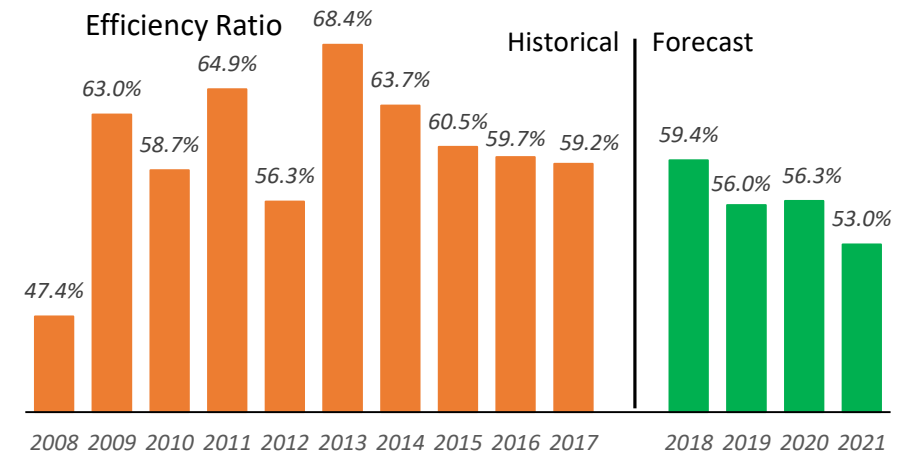
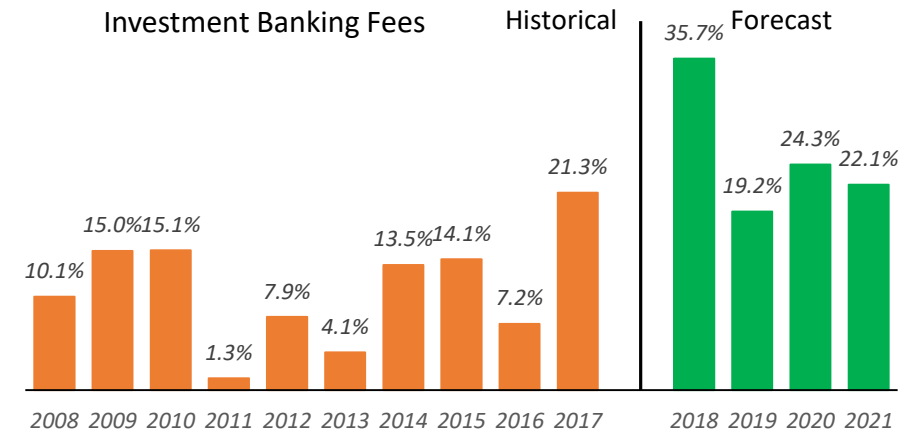
General Assumptions:

- Flat Yield Curve Environment (driven partially by low inflation expectations)
- Flat Yield Curve Environment also implies businesses are pessimistic about the future
- Growth in Net Interest Margins will remain slow/flat for the foreseeable future
- Flat yield curve will force SunTrust to purchase longer-term securities to take advantage of higher yields

Stronger IB Fees and Improved Efficiency Ratio

- SunTrust continues to grow its middle market and small company franchise
- Growth in Investment Banking fees led by equities underwriting and M&A deals
- SunTrust is also benefiting from its commercial banking division expanding into newer markets such as Texas and Ohio
- SunTrust earnings should benefit from growing middle market investment banking and improving efficiency ratio due to technological investments

Banking Operations



Source: Company Filings

Valuation



Valuation I: Comparable Companies Analysis

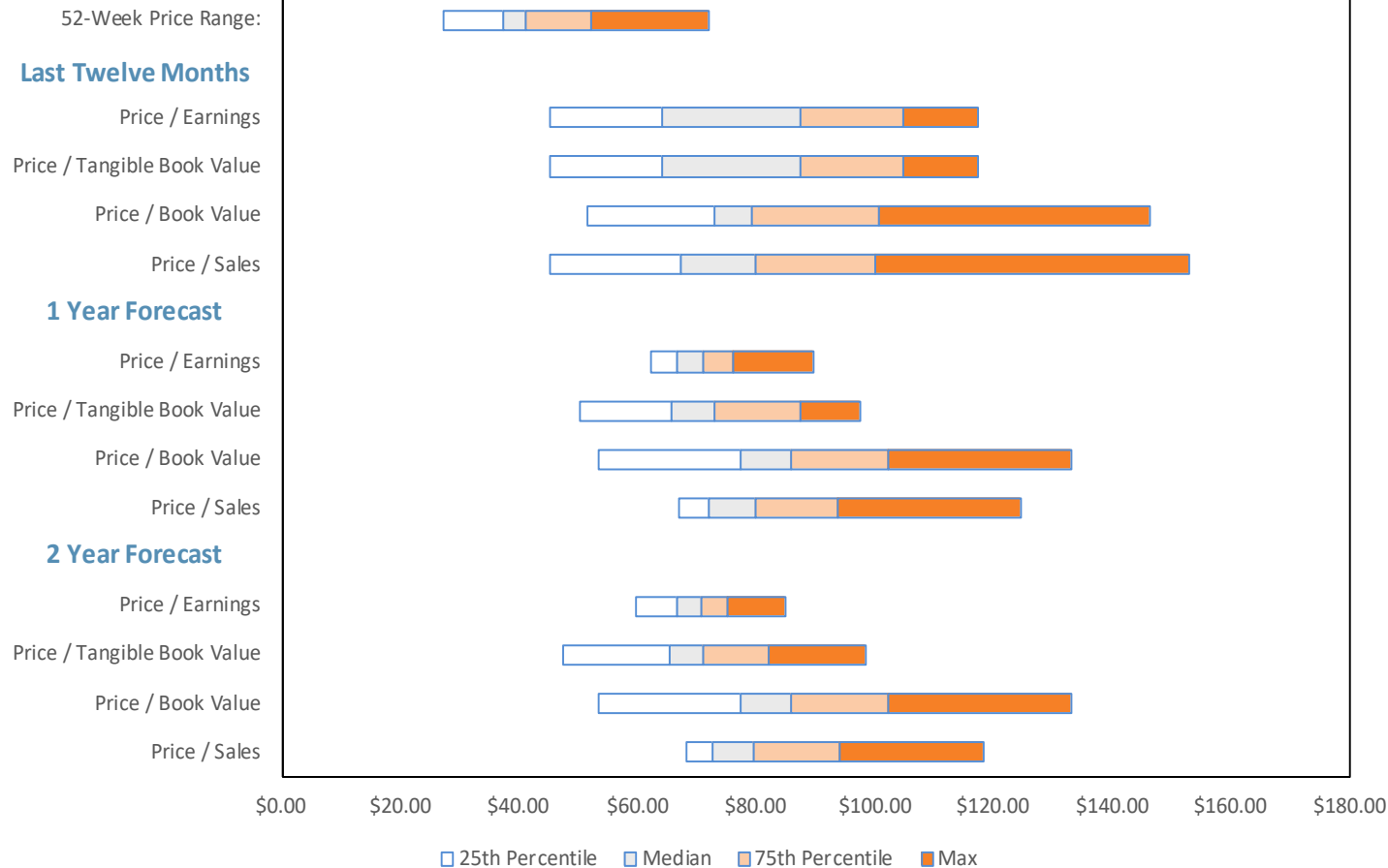


Trading Comps														
		Market Cap (mm)	Stock Price	Percentage of 52 Week High	Last Twelve Months				1 Year Forward				Return on Tanigble Common Equity	Dividend Yield
					P / S	P / B	P / TBV	P / E	P / S	P / B	P / TBV	P / E		
Retail Banking	Citizens Financial Group Inc	\$21,320	\$43.75	90.71%	2.98x	1.06x	1.62x	9.64x	3.50x	0.98x	1.55x	13.06x	17.09%	1.96%
	KeyCorp	\$22,833	\$21.16	95.23%	2.74x	1.63x	2.07x	14.99x	3.54x	1.56x	1.92x	12.60x	15.05%	0.51%
	M&T Bank Corp	\$28,889	\$192.19	97.38%	4.57x	1.92x	2.79x	19.03x	4.94x	1.83x	2.77x	15.86x	13.73%	1.86%
	BB&T Corp	\$43,156	\$54.95	97.79%	3.38x	1.62x	2.65x	20.33x	3.68x	1.57x	2.55x	14.02x	13.37%	2.93%
	Huntington Bancshares Inc/OH	\$16,960	\$15.82	95.70%	2.05x	1.74x	2.29x	9.18x	3.71x	1.59x	2.07x	13.07x	26.53%	3.25%
	Flushing Financial Corp	\$778	\$27.00	85.19%	3.68x	1.46x	1.65x	17.00x	4.15x	1.34x	1.42x	13.57x	3.68%	2.87%
	US Bancorp	\$91,395	\$55.01	94.03%	3.63x	2.07x	2.89x	11.39x	3.98x	1.82x	2.45x	13.52x	26.35%	2.57%
	Synovus Financial Corp	\$6,022	\$50.12	96.24%	4.29x	2.10x	2.21x	23.12x	4.21x	1.94x	2.07x	14.57x	9.61%	1.22%
	Wells Fargo & Co	\$297,338	\$59.21	89.29%	3.14x	1.64x	1.99x	15.60x	3.35x	1.61x	1.86x	12.47x	12.49%	3.05%
	Regions Financial Corp	\$22,027	\$19.62	97.61%	3.54x	1.43x	2.10x	20.11x	3.71x	1.39x	2.18x	14.64x	12.46%	1.99%
	Median			95.47%	3.46x	1.64x	2.16x	16.30x	3.71x	1.58x	2.07x	13.54x	13.55%	2.28%
WholeSale Banking	PNC Financial Services Group I	\$76,238	\$160.23	97.95%	4.52x	1.64x	2.02x	21.03x	4.43x	1.52x	2.09x	15.19x	10.23%	1.78%
	Fifth Third Bancorp	\$23,468	\$33.26	97.57%	2.75x	1.56x	1.87x	8.95x	3.64x	1.43x	1.87x	14.21x	21.88%	1.75%
	Zions Bancorporation	\$11,188	\$55.74	97.67%	3.73x	1.57x	1.83x	17.24x	4.07x	1.45x	1.82x	15.42x	11.29%	0.68%
	East West Bancorp Inc	\$9,589	\$66.34	95.80%	6.95x	2.54x	3.24x	21.23x	6.22x	2.43x	2.50x	15.08x	13.71%	1.21%
	SVB Financial Group	\$13,062	\$247.67	94.14%	5.45x	3.02x	3.02x	22.33x	5.63x	2.28x	2.65x	17.95x	13.85%	0.29%
	Comerica Inc	\$17,187	\$98.61	96.93%	4.75x	2.16x	2.35x	17.79x	5.05x	1.91x	2.30x	15.22x	13.70%	1.21%
	Median			97.25%	4.64x	1.90x	2.18x	19.41x	4.74x	1.72x	2.20x	15.20x	13.71%	1.21%
Target	SunTrust Banks Inc	\$33,106	\$70.57	97.18%	3.21x	1.46x	2.27x	13.93x	3.52x	1.29x	2.00x	14.11x	17.04%	2.66%
Peer Group (Average)					3.84x	1.80x	2.29x	16.64x	4.20x	1.64x	2.12x	14.38x	14.83%	1.87%

Valuation I: Comparable Companies Analysis



SunTrust Implied Price Per Share

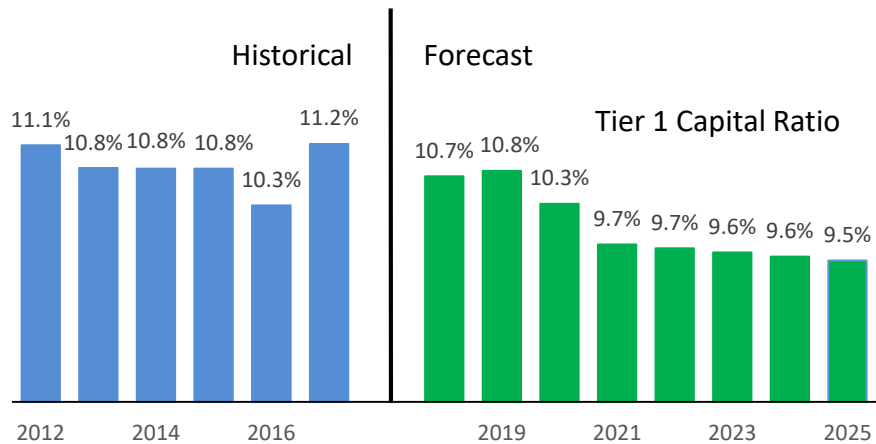
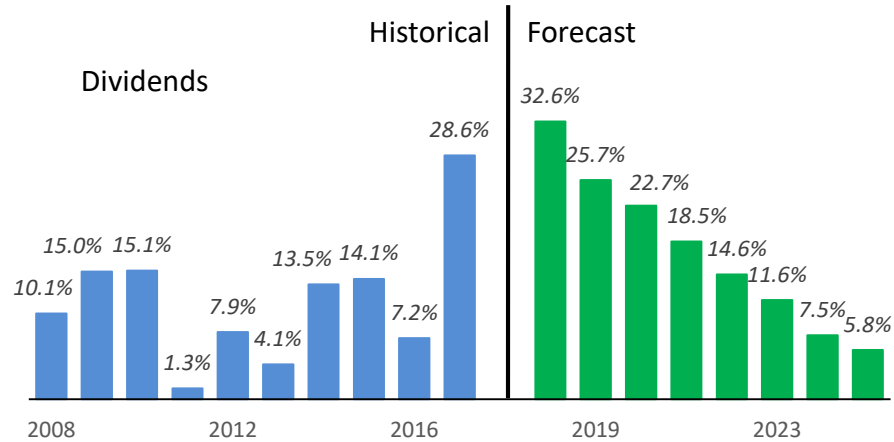


Valuation Summary:

- Current Price: **\$70.57**
- Price / Sales Value: **\$84.58**
- Price / Book Value: **\$87.10**
- Price / Tangible Book Value: **\$70.95**
- Price / Earnings Value: **\$84.31**

Valuation II: Dividend Discount Model

Tier 1 Capital Ratio / Dividend Forecast



Source: Company Filings

Dividend Growth Model Assumptions

- Previous 5 Year Growth Rate: 26.56%
- Dividends growing at an annual rate of 17.48% for 8 years before level of at 4% annually
- Net Income grows at an annual rate of 6.55% per year
- Shareholders Equity grows at an average annual rate of 5% *per year*
- Cost of Equity: 8.0%
- Risk-Weighted Assets Growth: 4.0%

Valuation II: Dividend Discount Model



Dividend Projections (In millions)

Fiscal year	2016 A	2017 A	2018A	2019 E	2020E	2021E	2022E	2023E	2024E	2025E
Fiscal year end date	12/31/2016	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021	12/31/2022	12/31/2023	12/31/2024	12/31/2025
Net Income to Common Shareholders'	\$1,942	\$1,882	\$2,273	\$2,356	\$2,470	\$2,816	\$3,259	\$3,266	\$3,428	\$3,584
% Growth	9.22%	(3.09%)	20.78%	3.66%	4.84%	13.99%	15.72%	0.23%	4.95%	4.57%
Dividends	\$475	\$499	\$634	\$842	\$1,059	\$1,300	\$1,540	\$1,789	\$2,004	\$2,153
% Growth	28.03%	4.98%	27.15%	32.86%	25.71%	22.73%	18.52%	16.14%	12.05%	7.42%
% Payout	24.46%	26.50%	27.89%	35.75%	42.87%	46.15%	47.27%	54.77%	58.48%	60.07%
Return on Equity	8.29%	7.97%	9.04%	8.84%	8.80%	9.51%	10.41%	10.43%	10.45%	10.48%
Total stockholders' equity - EOP	23,437	23,618	25,154	26,668	28,079	29,595	31,313	32,790	34,214	35,645
Less: Goodwill	(6,337)	(6,337)	(6,337)	(6,331)	(6,331)	(6,331)	(6,331)	(6,331)	(6,331)	(6,331)
Plus: Other	886	704	905	799	799	799	799	799	1,649	2,049
Tier 1 Capital - EOP	17,986	17,985	19,722	21,136	22,547	24,063	25,781	27,258	29,532	31,363
Tier 1 Capital Ratio	10.80%	10.28%	11.15%	11.79%	11.73%	11.16%	10.47%	10.23%	9.99%	9.74%

Dividend Discount Model Calculations

Discount Factor (Assumes Mid-year Adjustment)	96.24%	89.13%	82.55%	76.46%	70.81%	65.58%	60.74%
Present Value of Dividends	\$811	\$944	\$1,073	\$1,178	\$1,267	\$1,315	\$1,308

Perpetuity Growth Method	
Dividend Growth Rate	4.00%
Dividends _(t+1)	2,373,931
Terminal Value	59,144,225
Present Value of Terminal Value	33,175,541
Cumulative Present Value of Dividends	7,509,917
Equity Value	40,685,458
Shares Outstanding	477,422
STI Value Per Share	\$85.22
Market premium / (discount) to fair value	(12.99%)

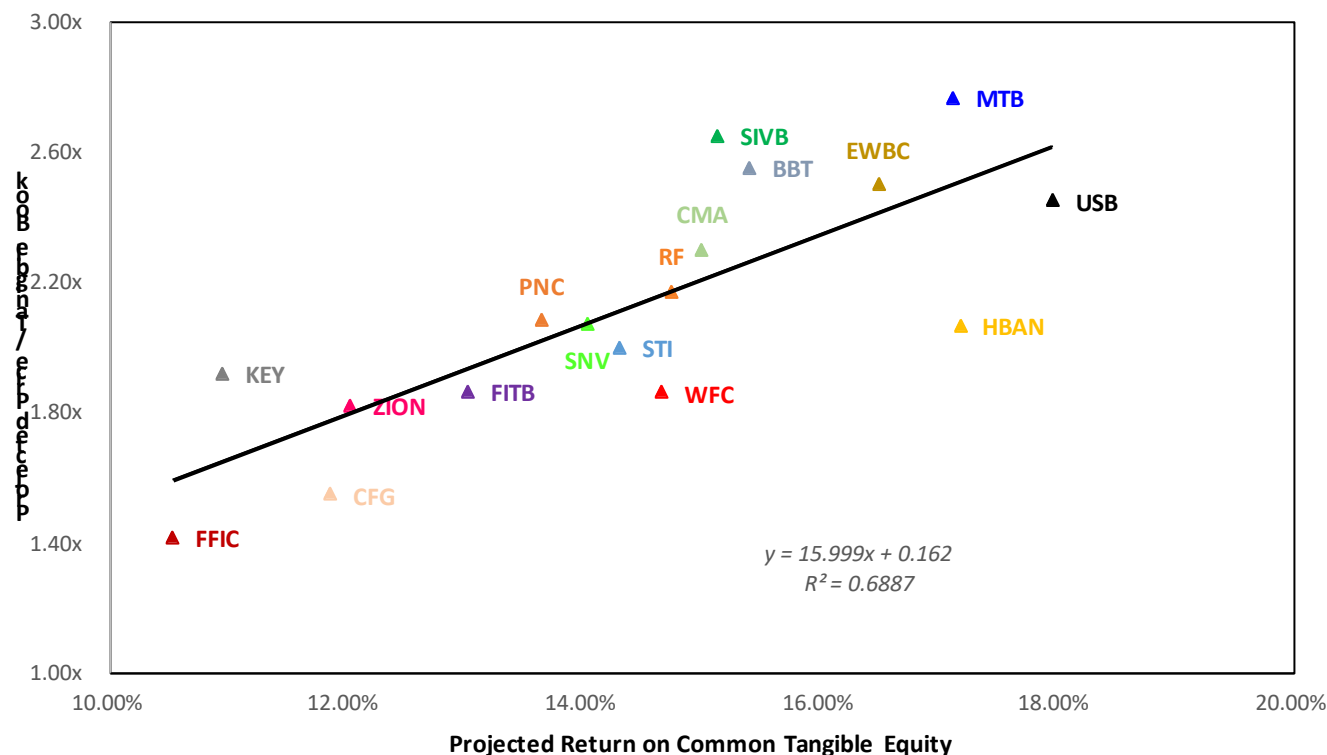
Exit Multiple Method	
Terminal Year Shareholders' Equity	34,374,492
Exit Multiple (Price / Book)	1.83x
Terminal Value	63,001,622
Present Value of Terminal Value	34,003,042
Cumulative Present Value of Dividends	7,509,917
Equity Value	41,512,959
Shares Outstanding	477,422
STI Value Per Share	\$86.95
Market premium / (discount) to fair value	(14.72%)

Note: In millions except for per share amounts; shares outstanding in thousands

Valuation III: Regression Analysis

Regression Valuation Analysis

Regression Analysis



- Used to sanity-check intrinsic and relative valuation analysis
- Correlation between Price / Tangible Book Value and Return on Common Tangible Equity
- More comparable companies will have a higher R^2 , vice-versa for less comparable firms
- Model implies companies with higher ROTCE should also trade at higher valuations

Implied Value Based on Linear Regression

Company Name	Ticker	Intercept	Slope	R^2	Projected Tangible Book Value FY 2018	Implied P / TBV FY 2018	Implied Equity Value (In Thousands)	Diluted Shares	Equity Value Per Share
SunTrust Banks Inc	STI	0.145	16.001	0.6647	16,530,500	2.43x	\$40,231,002	469,129	\$85.76

Valuation Summary



SunTrust Valuation Summary

Relative Valuation

LTM

Price / Earnings

Price / Book

Price / Tangible Book

Price / Sales

1 Year Forward

Price / Earnings

Price / Book

Price / Tangible Book

Price / Sales

Intrinsic Valuation

Exit Multiple

Dividend Discount Model

Regression Analysis

ROTCE | P / TBV



SunTrust Fair Value

- Based on all valuation metrics, SunTrust is undervalued
- Target Price: **\$89.11**
- Our target reflects a P/B multiple of 1.80x, an implied P/TBV multiple of 2.43x, and a long-term dividend growth rate of 4%

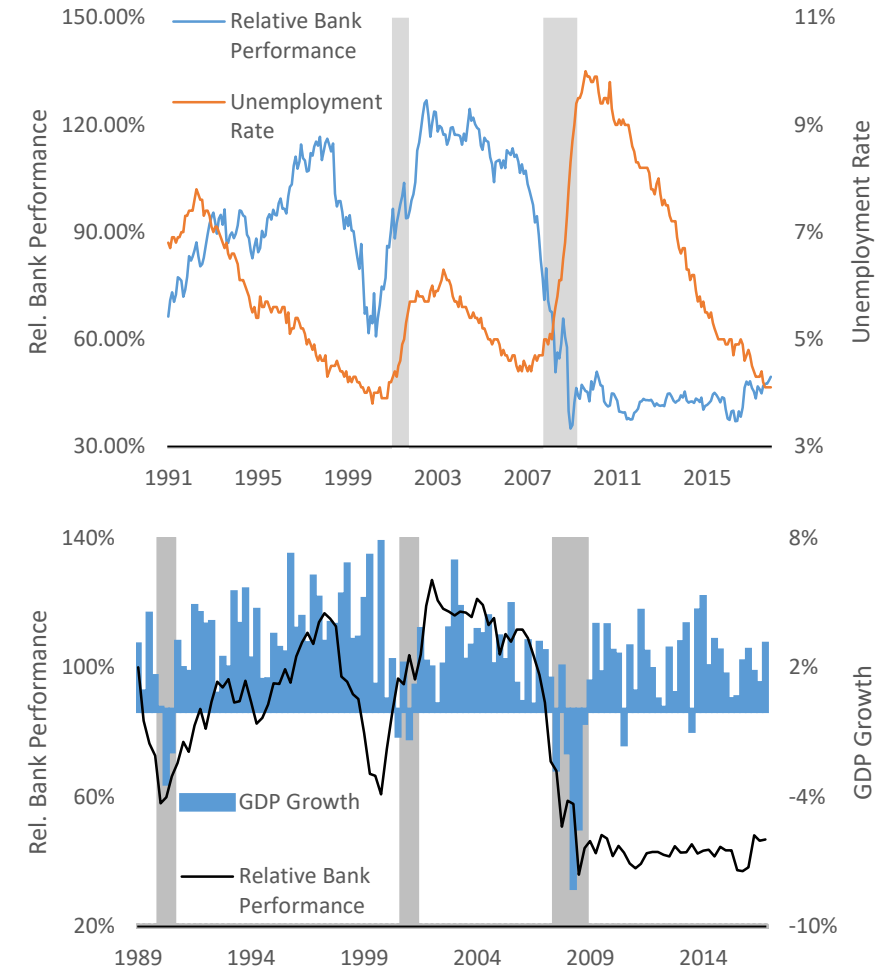
Risk Factors



Impact from Changing Economic Trends

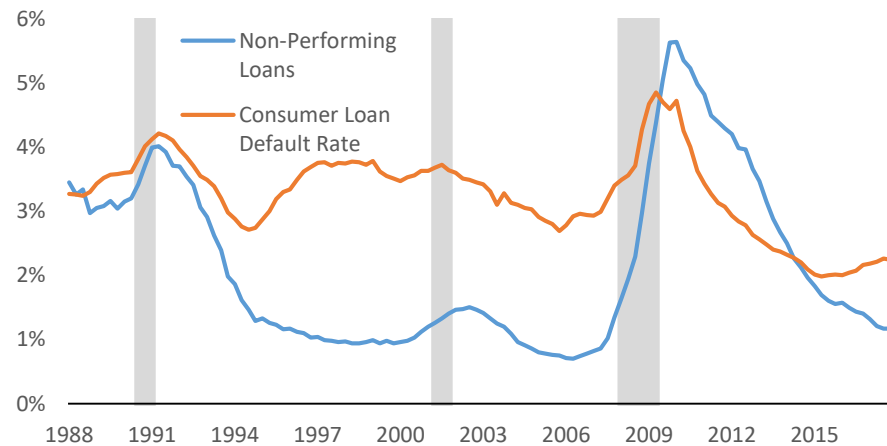
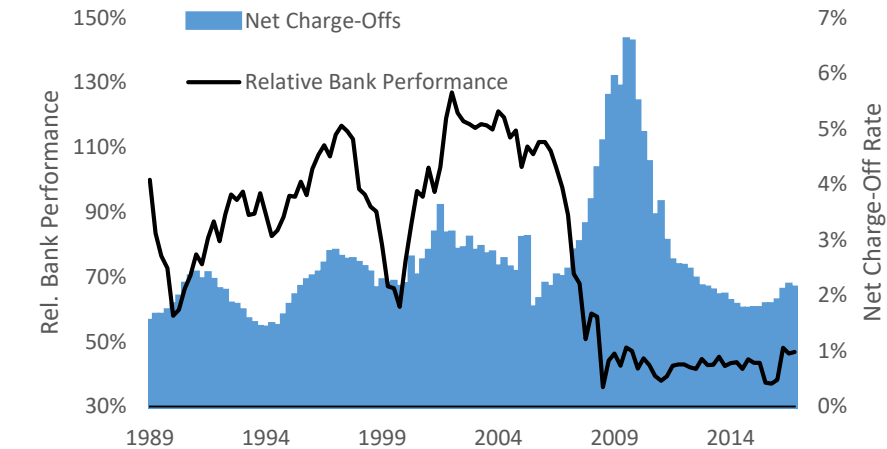
- Deterioration in economic conditions could affect SunTrust financial results or condition
- Slowing (or deteriorating) economic conditions could also erode consumer and investor confidence levels
- Bank stocks tend to outperform during booming economic times
- Although the chances of a recession are low, a declining economic environment would reduce loan growth

Bank Performance: Unemployment Rate / GDP Growth



Source: Bloomberg, Bureau of Labor Statistics, Bureau of Economic Analysis

Bank Performance: Net Charge-Offs / Non Performing Loans

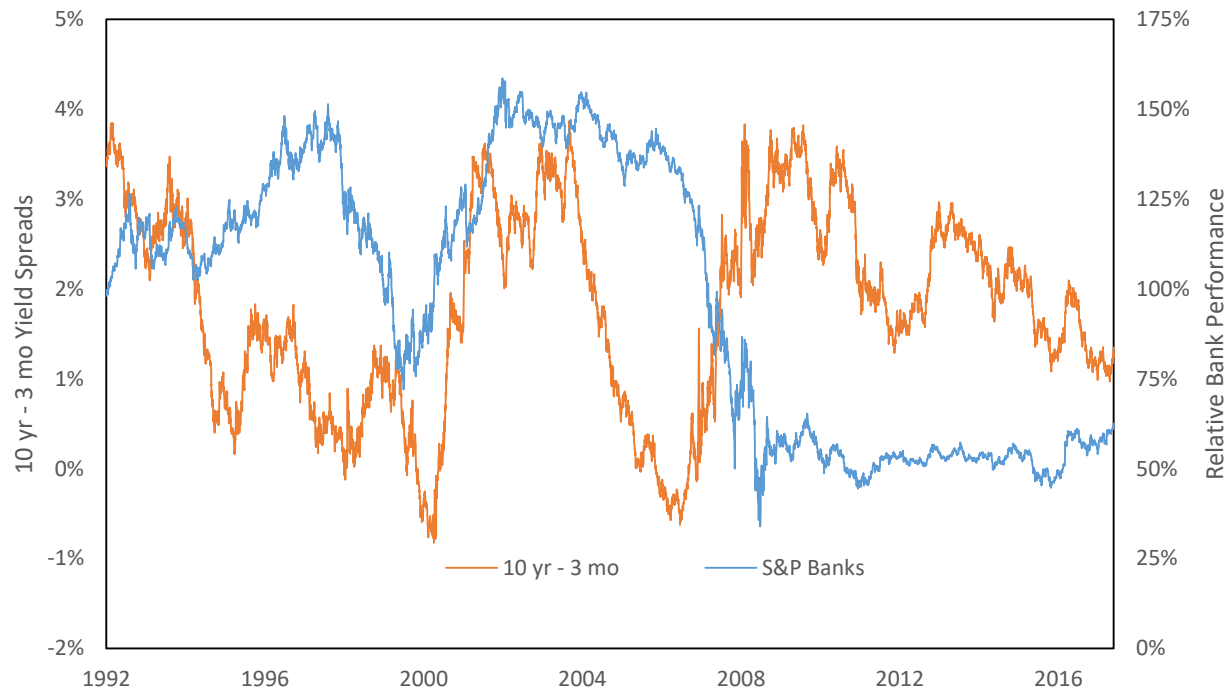


Source: Federal Reserve, Federal Institutions Examination Council

Impact from More Loan Defaults

- Net Charge-Offs are estimates of the amount of loans expected to default.
- Increases in the Net Charge-Off Rate imply more earnings pressure and occur during a weaker economy.
- Banks generally underperform during periods of rising credit cost
- Growing estimates in bad loans hurts earnings and capital as credit trends are likely to deteriorate
- Current Delinquency Rate: 2.24%

Yield Spreads & Bank Stock Performance



Source: Bloomberg

Impact from Large Interest Rate Fluctuations

- Changes in interest rates determine how quickly banks assets and liabilities change
- In general, bank stocks underperform when rates rise materially and outperform when rates decline sharply
- SunTrust estimates that it's equity value would decrease by -7.1% with a sudden 200 bp increase in rates

Relative bank stock performance during periods of rising 10-year rates

From	To	Δ in 2-Year Rates (bps)	Duration (Months)	Rate Levels		Stock Performance		
				Trough	Peak	Banks	S&P	Rel Perf.
8/21/1976	3/2/1980	898 bps	52	5.38%	14.09%	17%	29%	-12%
6/2/1980	10/1/1981	606 bps	16	9.78%	15.84%	-11%	4%	-17%
9/2/1988	10/16/1987	328 bps	14	10.92%	13.20%	-5%	18%	-23%
9/3/1988	13/21/1989	287 bps	13	7.05%	9.92%	13%	8%	5%
11/28/1988	4/17/1990	139 bps	51	8.64%	9.03%	-19%	-13%	-16%
3/9/1992	3/16/1992	123 bps	2	4.62%	5.85%	-5%	-3%	-8%
3/16/1992	10/22/1992	117 bps	24	3.66%	4.83%	11%	6%	5%
10/18/1998	12/29/1999	399 bps	15	3.78%	7.73%	-12%	-47%	-113%
2/14/1996	6/7/1996	164 bps	59	4.79%	6.43%	0%	0%	-0%
10/30/1998	5/19/2009	290 bps	19	4.00%	6.91%	-83%	32%	-409%
11/18/2001	4/2/2002	141 bps	5	2.36%	3.71%	12%	3%	9%
6/16/2003	6/29/2006	420 bps	37	1.08%	5.28%	25%	26%	-1%
3/5/2013	12/31/2013	140 bps	8	1.62%	3.02%	-17%	6%	-11%
5/8/2014	6/1/2015	110 bps	13	0.21%	1.31%	28%	30%	-2%
Average		280 bps	16			3%	11%	-8%

*Relative bank stock performance based on S&P Commercial Bank Index vs S&P 500 from 1989 - Present. Prior to that, S&P Financials Index was used.

Source: Bloomberg, S&P Capital IQ

Sudden Increases in Short-Term Rates

- Bank stocks (as well as bank profitability) is often threatened by sudden changes in interest rates
- Bank stocks significantly underperformed in 9 of the 14 periods when 2-year rates rose more than 130 basis points
- During periods of rising 2 year rates, banks have underperformed the S&P by -8% on average
- Banks underperformed -10% on average when considering rising 10 year rates

Overview

- Investing in SunTrust provides more than a 23% upside
- Wholesale banking and greater asset sensitivity should lead to greater profitability as the Federal Reserve prepares for its projected rate increases
- We expect SunTrust to successfully grow its investment banking business to drive revenue growth and manage its expenses and efficiency better than peers
- Assuming economic conditions remain unchanged, market risk, liquidity risk and interest rate risk should be minimal

Recommendation

- **Buy** SunTrust for ∞ shares...

