Title:
An Analysis of Valley National Bancorp (VLY)

Word Count:
1019

Summary:
A value investor discusses Valley National Bancorp (VLY). He looks at the bank's business and whether the stock is attractive at the current price.

Keywords:
vly, Valley, national, bancorp, bank, banks, banking, investing, value, stock, stocks, investor, finance

Article Body:

Valley National Bancorp (VLY) is a conservative bank with a strong position in northern New Jersey and a presence in Manhattan. The bank, founded in 1927, has about $12 billion in assets.

Valley has consistently earned extraordinary returns on assets and equity. Over the last twenty years, Valley has averaged a 1.74% return on assets and a 21.12% return on equity.

Valley’s worst two-year performance occurred in 1990 and 1991. During that period, Valley’s return on equity dropped as low as 14.54% and its ROA dropped as low as 1.29%. Even in Valley’s worst year (1991), the company still managed to roughly match the average long-term performance of most of its peers. In other words, Valley’s worst year was a close to typical year for many other banks.

It was at this low-point in 1991 that the board of directors decided not to increase the cash dividend. That was the only year in the last 37 that Valley did not increase its dividend.

The company has 79 consecutive years of profitable operations. That’s over 300 quarters (Valley has yet to post a quarterly loss). More importantly, Valley has a record of earning great returns on both assets and equity over long periods of time. So, what’s the company’s secret?

Location

Northern New Jersey is about the best place in the world to situate a bank. This isn’t hyperbole; if there’s a better location, I’ve yet to hear of it. As you know, American banks are unusually profitable. The market is large and highly fragmented. So, naturally the best place to situate a bank would be in the United States. But, why north Jersey in particular?

In a September 20th, 2001 interview with The Wall Street Transcript, Valley’s chairman, Gerald Lipkin, explained why northern New Jersey is such an attractive market:

"Northern New Jersey is the single most densely populated area on earth. There are more people per square mile in northern New Jersey than there are in India, China, Japan or anyplace else. We have the highest median family income in the United States in that area. So, we serve a very densely populated and affluent area, which is not dominated by any single industry."

Focus

Valley maintains a narrow focus both in terms of geography and services. The company’s offices are kept within one hour of the bank’s headquarters in Wayne, NJ. In the same interview, Mr. Lipkin explained why this geographic concentration is important: “We like to make it very convenient for our client base to meet with senior management as well as the other members of our staff."

Valley focuses on relationship banking. The company has residency requirements for its directors. The majority of directors are to live within 100 miles of the corporate headquarters. Furthermore, each board member is required to use Valley for both business and personal accounts. Theoretically, these two requirements ensure board members are familiar with the bank’s services and are best able to understand the needs of local businesses.

Discipline

Valley has a history of highly disciplined lending. Charge-offs are immaterial. Current reserves are adequate to cover many years of future charge-offs with little difficulty. The company’s asset quality ratios and loan to value ratios both indicate Valley has a more conservative approach to lending than many of its peers.

Undoubtedly, the local economy is helpful in this regard. Valley does not need to make questionable loans, because there is an abundance of opportunity in the local area. It is possible for the bank to remain fairly selective without forfeiting growth entirely. For instance, despite having $12 billion in assets, Valley only has about a 6% market share in northern New Jersey.

Management

Banking, like insurance, is a business where a particularly good or particularly poor management can greatly affect long-term results. The current Chairman, President, and CEO, Gerald Lipkin, has served for just over thirty years now. His record is unblemished.

Of course, the real responsibility for avoiding mistakes lies with others in the organization. There are few businesses where individual employees can do as much harm as they can within a bank. Valley’s past record and the level of experience of its top managers suggests investors should encounter very few unpleasant surprises resulting from human error.

Mr. Lipkin made his management philosophy quite clear with his concluding remarks in the aforementioned 2001 interview with The Wall Street Transcript:

"We never bet the ranch - we never put the bank in harms way on any single issue that could really harm it. Lending money is a risk taking business. So, obviously we at times have problems, situations with individual loans, but we try to avoid concentrations that could create major problems."

Valuation

Valley National Bancorp is a solid, well-run bank operating in a geographic area with excellent economics. The company’s physical footprint and its existing relationships give it a narrow moat in a highly profitable (and increasingly competitive) region.

Unfortunately, the company is trading at more than three times book. Three times book is a lot to pay for any bank. Valley’s future growth will likely be somewhat restrained by the company’s conservative approach. Therefore, dividends are going to make up a significant portion of an investor’s total returns.

Conclusion

Valley is a good bank. It has a real moat, albeit a narrow one. Competition is increasing within Valley’s territory. However, the company has been able to compete successfully with new entrants (who tend to take on far less profitable business).

The stock isn’t cheap today, but there is one wrinkle worth keeping in mind. Valley is more dependent upon interest rate spreads than most banks. If the yield curve was to become significantly steeper, Valley would reap outsized rewards.

The current dividend yield on a share of Valley National Bancorp is a little less than 3.5%. Considering the company’s limited growth prospects, this is an unattractive yield. If, during a period of general uncertainty within the banking industry, shares of VLY were to trade closer to two times book, investors would have an opportunity to make a long-term commitment in a quality bank.