



FINANCIAL SERVICES: OPPORTUNITIES IN A RISING RATE ENVIRONMENT

THE MONTHLY RESEARCH CONFERENCE CALL

MODERATOR:

Jim Kelleher, CFA

Director of Research

Wednesday, February 3, 2021

11:00 a.m. ET

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■ **Financial Services: Opportunities in a Rising Rate Environment**

- Jim Kelleher, CFA, Director of Research
- John Eade, President of Argus
- Stephen Biggar, Director of Financial Institutions Research
- Kevin Heal, Senior Analyst Financial Services

■ **Argus Quality Review**

- Comprehensive performance review of products & people
- Argus BUYs top the S&P 500 every year on a 1-year through 5-year period
- Bloomberg: Most analyst earn double-digit top 5 rankings
- Model Portfolios: 3 of 4 MPs beat benchmark on 1-yr, 3-year basis
- PS-FL: median stock return beats benchmark by 202 bps
- Find these on the homepage, News & Media

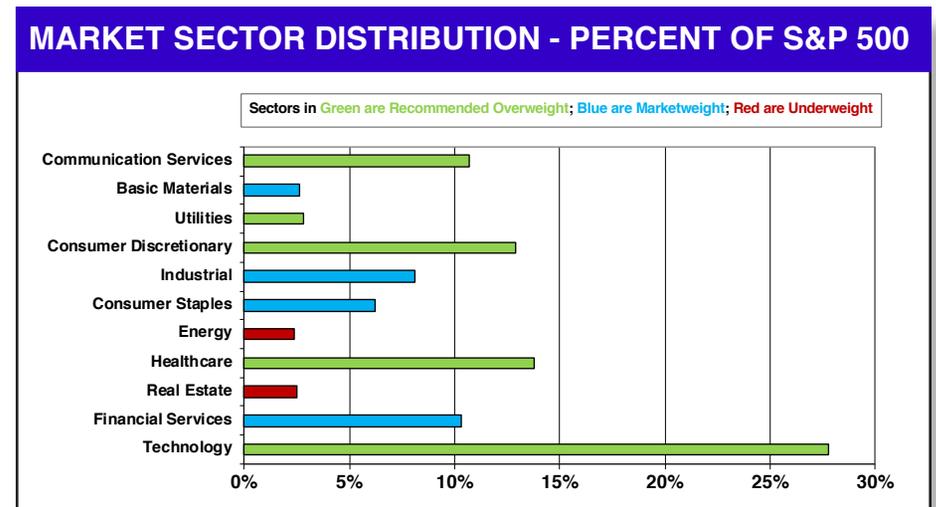
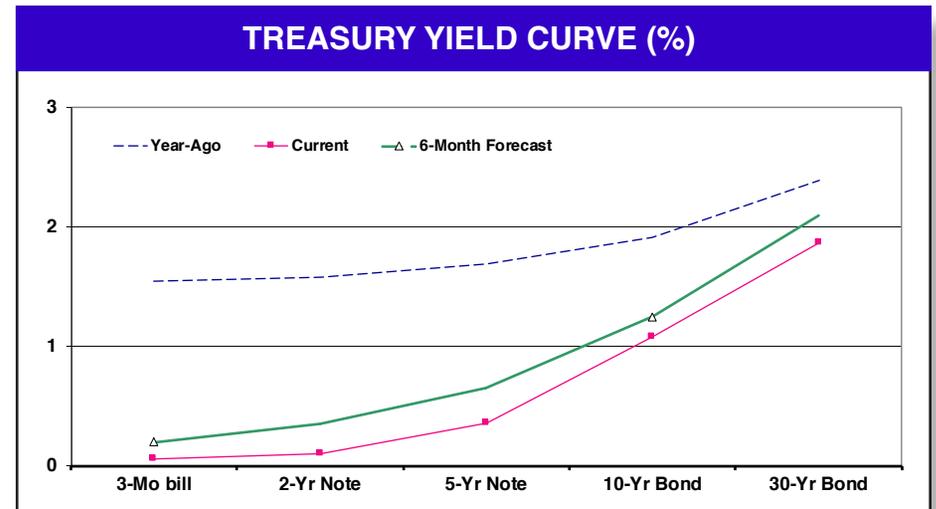
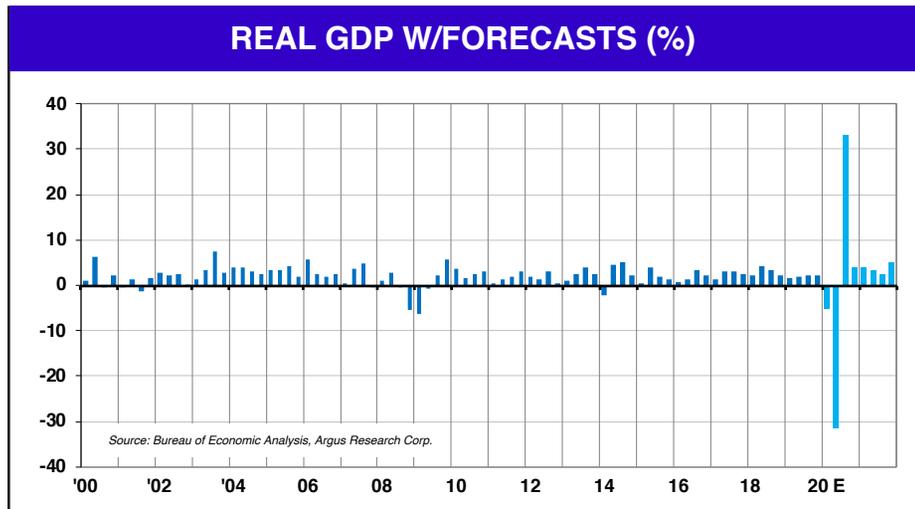
■ **Argus Quick Notes**

- New Coverage
- Energy Stock Values
- High Yield
- Top & Bottom Performers, 2020 & 4Q
- Find these on the homepage of our website

■ **Argus Mid-Cap Portfolio**

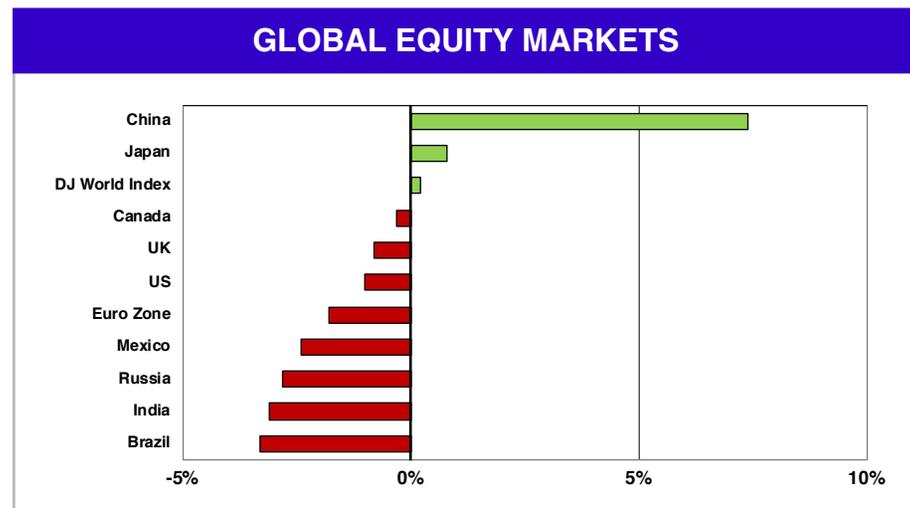
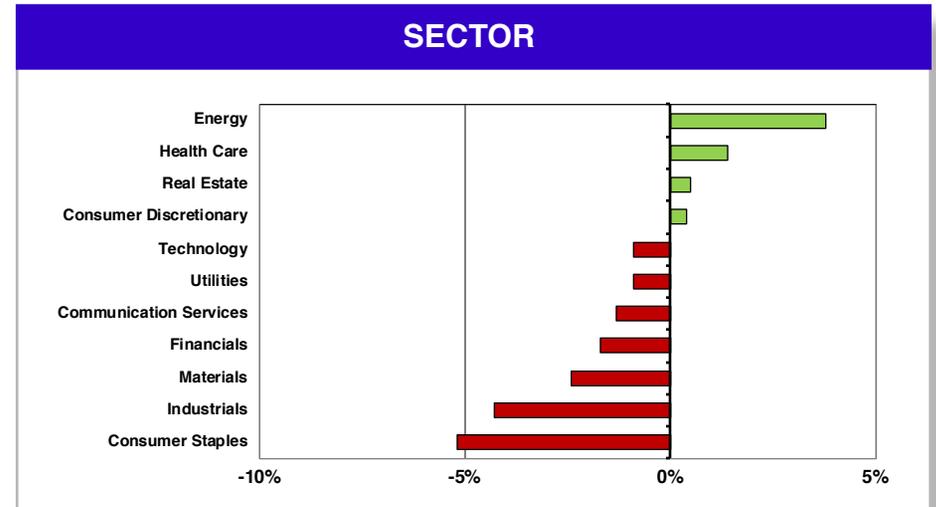
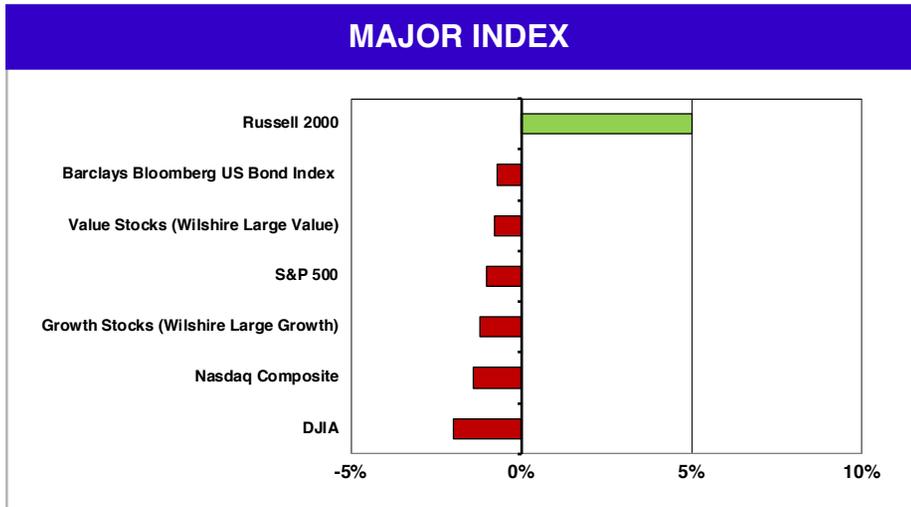
- Small & Mid-Cap (SMID) surged at year-end, into 2021
- Domestic focus makes them well-positioned as vaccines distributed
- Generally lower-priced than large-cap stocks
- Investors should have exposure to SMID stocks
- Find our Theme Portfolios under Portfolio Strategy on our website

MACRO FORECASTS



MARKET PERFORMANCE

DATA AS JANUARY 29, 2021



■ **Financial Sector noticeably underperformed in 2020 (-4% vs. +16%) on concerns over credit defaults and low interest rates, but has tracked broader market since December.**

• **Looking ahead, we believe tailwinds include:**

- » Recent uptick in 10-year yield has restored some steepness to the yield curve. Margins likely under pressure for only one more quarter (1Q21), with back half recovery.
- » Vaccine and business re-openings should lead to better loan growth, which paused during the pandemic.
- » Banks over-reserved in early part of pandemic with \$115 billion of loss provisions in the first half of 2020 when unemployment spiked to 15%. Likely to recapture in 2021.
- » Capital levels, which were healthy coming into the pandemic, strengthened further as buybacks and dividend increases were paused.
- » Continued strong contributions from fee-based revenue sources. While debt issuance may pause, we expect strong trading and investment banking to continue.

- **Diversified banks were relative outperformers in 2020 as trading and equity/debt issuance fees replaced lost lending revenues.**
- **We look for regional banks to offer more upside in 2021 as they are more sensitive to improvement in interest rates, loan growth and credit quality.**
- **Share buyback activity has already resumed with Fed approval, expect dividend increases to resume along with 2021/2022 CCAR results, further improving shareholder returns.**
- **Sector remains inexpensive on historical price-earnings/price-book ratios while offering historically high yields.**

■ PNC Financial Services (PNC: BUY)

- Well-diversified 18-state territory with a strong management team and stable credit risk profile.
- Proceeds from the May 2020 sale of BlackRock, Inc. (BLK) stake being used to acquire the U.S. banking subsidiary of Banco Bilbao Vizcaya (BBVA) for \$11.6 billion in cash.
- Purchase allows for geo expansion in the faster-growing Sunbelt region of the U.S., as well as a more coast-to-coast branch presence. Expect a healthy 21% earnings accretion in 2022 due to all cash purchase price and \$900 million of cost savings.
- Modest \$254 million recapture of loss provisions in 4Q (after provisions of \$3.4 billion in the first half of 2020) bodes well.

■ Truist Financial Corp. (TFC: BUY)

- Formed through the December 2019 merger of equals between BB&T Corp. and SunTrust Banks. With \$500 billion in assets, now ranks as the sixth-largest U.S. bank for both assets and deposits.
- Sharp drop in 4Q loss provisions a strong sign that loss reserves are now adequate for pandemic-related defaults.
- Merger synergies expected to result in above-peer-average ROE (20%+) and efficiency measures (low 50s).
- Combination has created a company with a steady growth profile, strong revenue diversification, and an above-average dividend yield, which merit a premium valuation.

■ U.S. Bancorp (USB: BUY)

- We believe stable revenue mix deserves an above-peer-average P/E. Payments business accounts for 16% of revenues (versus 5% for peers) while more volatile areas like trading, brokerage and investment banking represent just 3% (versus 13% for peers).
- Branch rationalization strategy expected to yield good results as USB closes 10%-15% of its branches by the end of 1Q21, while also adding branches in growth markets such as Charlotte.
- Loans grew an above-industry-average 3% in 4Q, and we see prospects for that continuing based on service territory.

■ Capital One Financial Corp. (COF: BUY)

- Large credit card issuer and consumer lender.
- High net charge-offs, feared in recent quarters due to pandemic-related job losses, have yet to materialize, as government stimulus programs and a more financially sound consumer heading into the pandemic have delayed defaults.
- Credit costs moderated in 4Q, with some loss reserves released back into earnings, as the company re-assessed expected default rates related to the pandemic.
- Encouragingly, COF noted opportunities for growth and expects to ramp up marketing spending from the more muted recent levels.

■ **Citizens Financial Group, Inc. (CFG: BUY)**

- Regional Bank in New England and Middle Atlantic Footprint.
- 4Q Noninterest Income up 17% with gains in mortgage banking and capital markets.
- Loss provisions much lower and expect some recovery in 2021.
- High current dividend of 4.3%. CEO indicated dividend is safe and potential stock buybacks resuming in 2021.

■ **The Allstate Corporation (ALL: BUY)**

- Continues to benefit from lower auto and homeowner claims.
- Recent sale of Allstate Life Insurance to Blackstone. Existing lower margin life and annuity policies.
- Dividend stable and share buybacks continued through pandemic.
- 3Q ROE of 17.7% above management goal of 14%-17%.

■ **AGNC Investment Corp. (AGNC: BUY)**

- Leveraged residential mortgage REIT.
- Purchases Gov't-backed mortgages on a leveraged basis. Federal Reserve continues to support this market by purchasing at least \$40 billion per month.
- Current leverage is 8.4x.
- Book value over \$17.00 as of Mid-January.
- Dividend yield approximately 9.0%.

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