

Ally Financial Inc. (ALLY)

\$19.05 (As of 07/09/20)

Price Target (6-12 Months): **\$20.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/14/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:D

Value: B

Growth: F

Momentum: D

Summary

Ally Financial's shares have underperformed the industry so far this year. The company's earnings surpassed the Zacks Consensus Estimate in two and met in one of the trailing four quarters. Mounting expenses (mainly owing to its inorganic expansion initiatives) are expected to continue hampering bottom-line growth to some extent. Presence of high levels of debt and deteriorating credit quality remain major concerns. Notably, due to the uncertainties related to the virus, the company has called off the deal to acquire CardWorks. However, the company's efforts to diversify revenues, increase in consumer loan demand and strong capital position will likely support profitability. Moreover, its inorganic growth initiatives poise it well for the future. The company's capital deployment activities will likely enhance shareholder value.

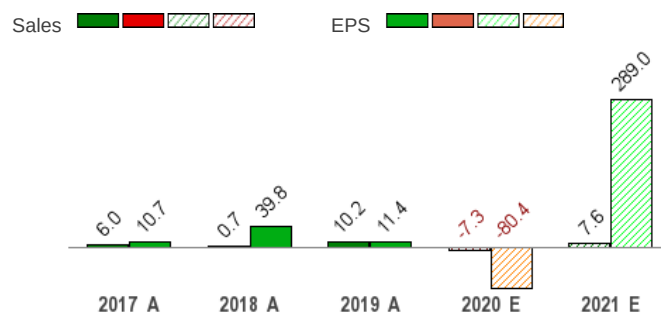
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$35.42 - \$10.22
20 Day Average Volume (sh)	5,887,520
Market Cap	\$7.1 B
YTD Price Change	-37.7%
Beta	1.62
Dividend / Div Yld	\$0.76 / 4.0%
Industry	Financial - Consumer Loans
Zacks Industry Rank	Bottom 29% (179 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-163.8%
Last Sales Surprise	-12.0%
EPS F1 Est- 4 week change	-12.1%
Expected Report Date	07/17/2020
Earnings ESP	-88.8%
P/E TTM	7.7
P/E F1	26.1
PEG F1	1.9
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,556 E	1,520 E	1,575 E	1,639 E	6,378 E
2020	1,412 A	1,464 E	1,481 E	1,574 E	5,930 E
2019	1,598 A	1,552 A	1,601 A	1,643 A	6,394 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.40 E	\$0.56 E	\$0.77 E	\$0.91 E	\$2.84 E
2020	-\$0.44 A	\$0.31 E	\$0.40 E	\$0.46 E	\$0.73 E
2019	\$0.80 A	\$0.97 A	\$1.01 A	\$0.95 A	\$3.72 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 07/09/2020. The reports text is as of 07/10/2020.

Overview

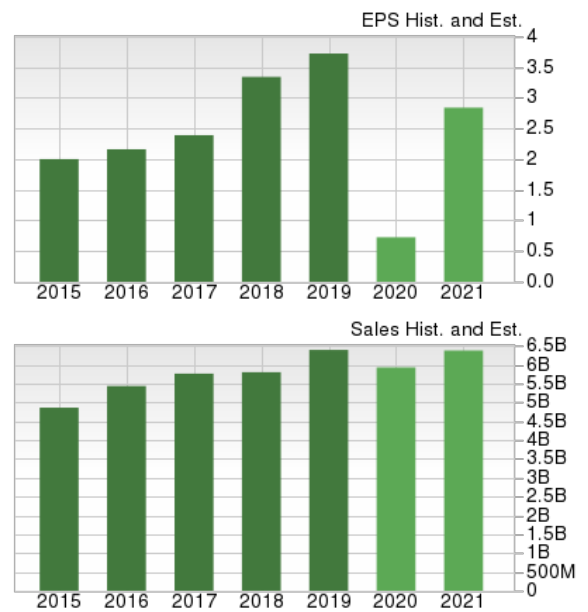
Founded in 1919, Detroit, MI-based Ally Financial Inc. is a diversified financial services company providing a broad array of financial products and services, primarily to automotive dealers and their customers. It operates as a financial holding company (FHC) and a bank holding company (BHC). Ally Bank is an indirect, wholly-owned banking subsidiary of Ally Financial.

The company operates through the following four business segments:

- **Automotive Finance** (comprising 68.7% of total net revenues in 2019) provides retail installment sales financing, loans, and leases; term loans and other lines of credit to dealers; fleet financing, and vehicle remarketing services to consumers and automotive dealers.
- **Insurance** (20.8%) offers both consumer finance protection and insurance products. It also provides consumer financial and insurance products and underwrites selected commercial insurance coverages.
- **Mortgage Finance** (3.0%) includes the management of the company's held-for-investment consumer mortgage loan portfolio.
- **Corporate Finance** (4.4%) provides senior secured leveraged cash flow and asset-based loans largely to U.S.-based middle market companies.

Corporate and Other (3.1%) consists of centralized corporate treasury activities, the residual impacts of corporate funds-transfer pricing, asset liability management activities and the amortization of the discount associated with debt issuances and bond exchanges.

In 2016, Ally Financial acquired TradeKing, a digital wealth management firm. In 2019, the company acquired Health Credit Services LLC.



Reasons To Buy:

- ▲ Growth in one of the key sources of revenues – total financing revenues and other interest income – remains a major positive for Ally Financial. It witnessed a CAGR of 4.1% over the last five years (2015-2019). While the same declined in the first quarter of 2020; strong origination volumes, retail loan growth and rise in deposit balances are expected to keep the momentum intact.
- ▲ Ally Financial has been witnessing a steady improvement in net interest margin (NIM) over the past several years. While NIM declined slightly in first-quarter 2020 due to lower interest rates, the same has grown from 1.40% in 2012 to 2.67% in 2019. In fact, rising consumer loan demand and management's efforts to become a diversified banking company are expected to continue to offer support in the near term despite near-zero interest rates, which might offset NIM growth to some extent.
- ▲ As part of its strategy to diversify into banking products, Ally Financial has forayed into the mortgage business, which is supporting the company's earnings growth. The company has also been making efforts to enhance digital offerings and introduce products to further boost its profitability. Notably, its wealth management and online brokerage initiatives related to the credit card offerings remain impressive. Also, acquisitions of TradeKing and Health Credit Services (a point-of-sale payment provider) will aid in improving its product offerings.
- ▲ Ally Financial has come a long way in improving its balance sheet and fundamentals. This has resulted in the company's robust capital deployment actions. In January 2020, the company announced 11.8% dividend hike. This followed two hikes – 13.3% in January 2019 and 15.4% in July 2018. Also, the company had share repurchase authorization in place, which it has currently suspended amid the coronavirus outbreak. Nevertheless, driven by its capital strength, earnings growth and favorable dividend payout ratio, the company will be able to sustain enhanced capital deployment activities.
- ▲ Further, Ally Financial seems undervalued compared with the broader industry. Its current price/book and price/cash flow ratios are lower than the respective industry averages. The stock has a Value Score of B.

Ally Financial's initiatives to diversify revenue base and rise in demand for consumer loans will aid profitability. Given a solid balance sheet, it is well poised to expand through acquisitions.

Reasons To Sell:

- ▼ Ally Financial has been witnessing a persistent rise in expenses. Over the last five years (ended 2019), expenses witnessed a CAGR of 5.6%, with the uptrend continuing in the first quarter. With the company launching products, seeking opportunistic buyouts and expanding into newer areas of operations, expenses are expected to remain elevated.
- ▼ Worsening asset quality is a headwind for Ally Financial. Although the company's provision for loan losses and net-charge offs (NCOs) declined in 2018, the same witnessed a CAGR of 9% and 12.5%, respectively, over the last five years (2015-2019). Moreover, owing to the concerns related to the coronavirus outbreak, both provisions and NCOs witnessed a rise in the first quarter of 2020. Steadily deteriorating credit quality is expected to dampen the company's financials.
- ▼ As of Mar 31, 2020, Ally Financial had total debt worth \$40.6 billion, significantly higher than the cash and cash equivalents balance of \$6.2 billion. Moreover, interest expenses on long-term debt constituted 24.6% of its total net revenues in first-quarter 2020. While the company's total debt to total capital of 69.7% has declined in the first quarter on a sequential basis, it compares unfavorably with the industry average of 67.7%. Further, its current times-interest-earned ratio of 1.7 declined from the prior quarter and is lower than the industry average of 2.7. Thus, we believe that such high levels of debt may negatively impact its access to liquidity and increase borrowing costs in the unsecured market. Also, the company's current liquidity position might not be sufficient to meet debt obligations if economic situation worsens.
- ▼ Ally Financial's trailing 12-month return on equity (ROE) undercuts its growth potential. The company's ROE of 6.92% compares unfavorably with ROE of 13.91% for the industry, reflecting that it is less efficient in using shareholder funds.
- ▼ Shares of Ally Financial have underperformed the industry so far this year. Also, the company's 2020 earnings estimates have been unchanged over the past seven days. Therefore, given the above-mentioned concerns and lack of positive estimate revisions, the stock has limited upside potential.

Continuously rising expenses are expected to hurt Ally Financial's bottom-line growth. Deteriorating credit quality and presence of high level of debt might hamper the company's financials.

Last Earnings Report

Ally Financial Posts Q1 Loss on Higher Provisions & Costs

Ally Financial's first-quarter 2020 adjusted loss was 44 cents per share against the Zacks Consensus Estimate for earnings of 71 cents. The figure deteriorated from the year-ago quarterly earnings of 80 cents per share.

Results reflected substantial reserve build to combat coronavirus-related concerns, which in turn resulted in increase in credit costs. Further, decline in revenues, rise in operating expenses and lower loan balance were headwinds. However, growth in deposit balance was impressive.

After considering non-recurring items, net loss available to common shareholders (on a GAAP basis) was \$319 million or 85 cents per share versus net income of \$374 million or 92 cents per share recorded in the prior-year quarter.

Revenues Down, Expenses Rise

Total net revenues were \$1.41 billion, declining 28.5% year over year. The figure also lagged the Zacks Consensus Estimate of \$1.61 billion.

Net financing revenues were up 1.2% from the prior-year number to \$1.15 billion. The rise was driven by higher retail auto portfolio yield and balance, and liability mix shift, which were partly offset by lower commercial auto balance and portfolio yield.

Adjusted net interest margin was 2.68%, down 1 basis point (bps).

Total other revenues of \$266 million declined 42.9% from the prior-year level.

Total non-interest expenses increased 10.8% year over year to \$920 million. The rise was mainly due to an increase in all cost components.

Adjusted efficiency ratio at the end of the first quarter was 52.3%, up from 48.9% recorded in the comparable year-ago period. A rise in efficiency ratio indicates deterioration in profitability.

Credit Quality Worsens

Non-performing loans of \$1.46 billion as of Mar 31, 2020 were up 47.7% from the corresponding period of 2019. Further, net charge-off rate was 0.84%, up 11 bps.

Also, provision for loan losses surged to \$903 million from \$282 million recorded in the prior-year quarter. The drastic increase was due to reserve build, primarily driven by coronavirus-induced economic slowdown.

Strong Balance Sheet & Capital Ratios

Total net finance receivables and loans amounted to \$124.9 billion as of Mar 31, 2020, decreasing 1.6% from the fourth quarter. Deposits totaled \$122.3 billion, increasing 1.3% sequentially.

As of Mar 31, 2020, total capital ratio was 12.8%, improving from 12.5% in the comparable period of last year. Tier I capital ratio was 10.9% as of Mar 31, 2020, down from 11.0% in the corresponding period of 2019.

Share Repurchases

During the quarter, the company repurchased shares worth \$104 million. However, in mid-March, it suspended the share buyback plan through second-quarter 2020 amid coronavirus concerns.

2020 Outlook

The company has withdrawn its 2020 outlook in response to the uncertainties related to the coronavirus outbreak.

Retail auto NCO rate is projected at 1.8-2.1%.

Quarter Ending 03/2020

Report Date	Apr 20, 2020
Sales Surprise	-11.99%
EPS Surprise	-163.77%
Quarterly EPS	-0.44
Annual EPS (TTM)	2.49

Recent News

Ally Financial-CardWorks Merger Deal Mutually Terminated - Jun 24, 2020

Ally Financial announced that the acquisition of CardWorks, a credit card issuer with focus on the "non-prime" segment, has been called off due to the uncertainties related to the coronavirus pandemic.

The acquisition deal, announced this February, was likely to close in the third quarter of 2020. Ally Financial was expected to fund the transaction with \$1.35 billion in cash and \$1.30 billion in its common stock, amounting to a total consideration of \$2.65 billion. As the deal has been mutually terminated, neither of the parties needs to pay any termination or break-up fee.

Don Berman, CardWorks chief executive officer said, "After careful consideration, Jeff Brown and I, along with our boards of directors, concluded that it would be in the best interest of our customers and our stakeholders, to terminate the agreement." The boards of both companies have approved the termination.

Dividend Update

On Apr 16, Ally Financial declared a quarterly dividend of 19 cents per share. The dividend was paid out on May 15 to shareholders of record as of May 1.

Valuation

Ally Financial's shares are down 37.6% in the year-to-date period and 39.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 34.5% and 20.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are down 31.7% and 16.1%, respectively.

The S&P 500 index is down 1.4% in the year-to-date period but up 6.1% over the past year.

The stock is currently trading at 10.51X forward 12 months earnings, which compares to 11.87X for the Zacks sub-industry, 16.14X for the Zacks sector and 22.62X for the S&P 500 index.

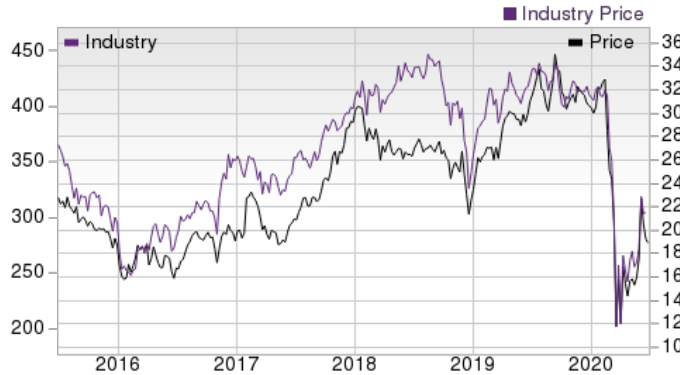
Over the past five years, the stock has traded as high as 18.07X and as low as 2.68X, with a 5-year median of 8.03X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$20 price target reflects 11.05X forward earnings.

The table below shows summary valuation data for ALLY

Valuation Multiples - ALLY					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	10.51	11.87	16.14	22.62
	5-Year High	18.07	13.16	16.27	22.62
	5-Year Low	2.68	4.39	11.59	15.27
	5-Year Median	8.03	8.77	14.18	17.59
P/TB TTM	Current	0.53	0.78	3.26	12.51
	5-Year High	1.02	1.54	3.95	13.49
	5-Year Low	0.31	0.51	2.05	6.34
	5-Year Median	0.78	1.2	3.46	9.6
P/S F12M	Current	1.15	0.98	6.04	3.53
	5-Year High	2.27	1.97	6.7	3.53
	5-Year Low	0.65	0.72	4.96	2.52
	5-Year Median	1.75	1.49	6.07	3.04

As of 07/09/2020

Industry Analysis Zacks Industry Rank: Bottom 29% (179 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Credit Acceptance Corporation (CACC)	Outperform	1
MR. COOPER GROUP INC (COOP)	Neutral	2
First Cash, Inc. (FCFS)	Neutral	3
Huntington Bancshares Incorporated (HBAN)	Neutral	3
LexinFintech Holdings Ltd. Sponsored ADR (LX)	Neutral	5
Santander Consumer USA Holdings Inc. (SC)	Neutral	4
Navient Corporation (NAVI)	Underperform	5
SLM Corporation (SLM)	Underperform	4

Industry Comparison Industry: Financial - Consumer Loans				Industry Peers		
	ALLY	X Industry	S&P 500	CACC	NAVI	SC
Zacks Recommendation (Long Term)	Neutral	-	-	Outperform	Underperform	Neutral
Zacks Rank (Short Term)	5	-	-	1	5	4
VGM Score	D	-	-	D	A	B
Market Cap	7.11 B	639.37 M	21.19 B	7.36 B	1.25 B	5.56 B
# of Analysts	6	2	14	3	3	6
Dividend Yield	3.99%	0.00%	1.96%	0.00%	9.89%	5.08%
Value Score	B	-	-	D	A	A
Cash/Price	0.85	0.75	0.07	0.07	2.82	0.43
EV/EBITDA	6.12	6.19	12.56	10.82	99.35	9.40
PEG Ratio	1.97	2.27	2.85	NA	NA	NA
Price/Book (P/B)	0.53	0.97	3.00	3.85	0.61	1.08
Price/Cash Flow (P/CF)	2.39	3.05	11.41	11.52	2.25	2.02
P/E (F1)	26.64	12.02	20.79	49.05	2.96	NA
Price/Sales (P/S)	1.15	0.79	2.19	4.83	0.25	0.70
Earnings Yield	3.83%	7.04%	4.52%	2.04%	33.85%	-0.52%
Debt/Equity	2.30	2.30	0.76	2.42	39.70	7.82
Cash Flow (\$/share)	7.96	4.49	6.94	36.22	2.88	8.57
Growth Score	F	-	-	D	C	D
Hist. EPS Growth (3-5 yrs)	15.39%	10.98%	10.90%	24.10%	6.79%	1.28%
Proj. EPS Growth (F1/F0)	-80.51%	-33.74%	-9.99%	-75.39%	-17.17%	-102.97%
Curr. Cash Flow Growth	-1.59%	14.13%	5.51%	18.61%	12.54%	20.07%
Hist. Cash Flow Growth (3-5 yrs)	-4.75%	9.07%	8.55%	19.03%	-5.09%	25.86%
Current Ratio	0.99	3.42	1.30	28.62	10.48	63.41
Debt/Capital	69.68%	68.95%	44.46%	70.76%	97.54%	88.66%
Net Margin	16.46%	8.29%	10.62%	26.76%	7.24%	9.32%
Return on Equity	6.92%	13.91%	15.75%	30.52%	18.83%	10.95%
Sales/Assets	0.03	0.24	0.55	0.21	0.05	0.17
Proj. Sales Growth (F1/F0)	-7.26%	-0.05%	-2.52%	0.75%	-5.28%	0.34%
Momentum Score	D	-	-	F	A	B
Daily Price Chg	-3.15%	-3.90%	-1.52%	-4.25%	-6.10%	-5.62%
1 Week Price Chg	3.24%	0.67%	3.66%	2.61%	-1.15%	-2.13%
4 Week Price Chg	1.06%	-5.38%	0.36%	-0.83%	-13.04%	-4.36%
12 Week Price Chg	40.49%	27.46%	10.41%	46.29%	-10.26%	37.06%
52 Week Price Chg	-39.87%	-33.33%	-8.70%	-14.74%	-51.39%	-32.91%
20 Day Average Volume	5,887,520	345,453	2,339,510	171,198	4,722,017	971,260
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-12.12%	0.00%	0.00%	0.00%	0.00%	32.00%
(F1) EPS Est 12 week change	-80.03%	-39.97%	-7.77%	69.53%	-29.33%	-103.45%
(Q1) EPS Est Mthly Chg	-10.17%	0.00%	0.00%	0.00%	0.00%	30.39%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	F
Momentum Score	D
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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