

ETRADE Financial (ETFC)

\$53.37 (As of 08/17/20)

Price Target (6-12 Months): **\$56.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/10/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:F

Value: D

Growth: F

Momentum: C

Summary

Shares of E*TRADE have outperformed the industry over the past three months. Also, the company has an impressive earnings surprise history, surpassing the Zacks Consensus Estimate in three of the trailing four quarters and missed in one. The second-quarter 2020 results reflected higher revenues, improved DARTs, rise in customer accounts and benefit provision, along with escalating expenses and margin pressure. Continued improvement in DARTs on increased market volatility acts as a tailwind. Balance-sheet restructuring and strong liquidity position are positive factors. E*TRADE faces less credit risk in case of any economic downturn. Yet, the company's rising expenses are a concern. Further, low rates are likely to impede the company's revenue growth. Also, significant dependence on interest-based revenues streams keeps us apprehensive.

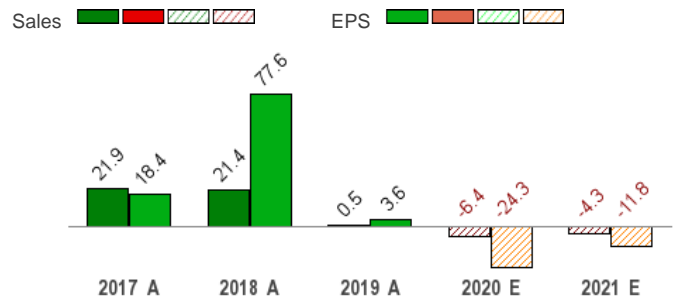
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$57.30 - \$25.76
20 Day Average Volume (sh)	1,753,159
Market Cap	\$11.8 B
YTD Price Change	17.6%
Beta	1.25
Dividend / Div Yld	\$0.56 / 1.0%
Industry	Financial - Investment Bank
Zacks Industry Rank	Top 29% (74 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	17.3%
Last Sales Surprise	5.6%
EPS F1 Est- 4 week change	6.9%
Expected Report Date	10/15/2020
Earnings ESP	1.5%
P/E TTM	14.7
P/E F1	17.5
PEG F1	1.6
P/S TTM	4.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	638 E	637 E	639 E	644 E	2,583 E
2020	707 A	716 A	664 E	629 E	2,700 E
2019	755 A	685 A	767 A	679 A	2,886 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.63 E	\$0.68 E	\$0.65 E	\$0.70 E	\$2.69 E
2020	\$0.82 A	\$0.88 A	\$0.71 E	\$0.73 E	\$3.05 E
2019	\$1.09 A	\$1.12 A	\$1.08 A	\$0.84 A	\$4.03 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 08/17/2020. The reports text is as of 08/18/2020.

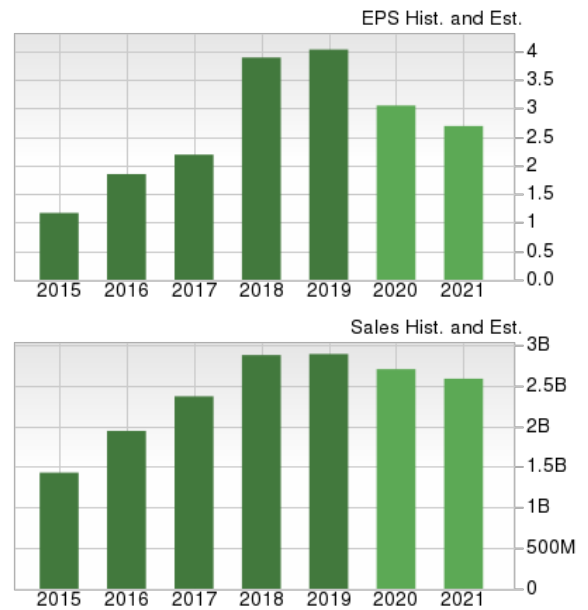
Overview

Founded in 1982 in California and headquartered in New York, E*TRADE Financial Corporation provides online brokerage and related products and services primarily to individual retail investors, under the brand name of “E*TRADE Financial” worldwide. The company was reincorporated in Delaware in July 1996. Along with its subsidiaries, E*TRADE offers various brokerage products and services including automated order placement and execution of the U.S., as well as international equities, currencies, futures, options, exchange-traded funds, mutual funds, and bonds. The banking products and services include checking, savings and clearing facilities, along with money market and certificates of deposit products. E*TRADE operates worldwide, primarily in the U.S., Europe and Asia. The company provides these services to customers online through its network of customer service representatives, investment professionals, and investment advisors – over the phone and in person in all of its 30 E*TRADE branches.

Previously, the company operated through two reporting segments – *Trading and Investing* and *Balance Sheet Management*. However, the company made several reporting changes in the first quarter of 2016 including consolidation of its reporting segments. Given that most of the company’s legacy costs are behind it and balance sheet strength now depends on maximizing the value of customer deposits, management viewed that it was the right time to terminate the balance sheet management segment as well as the corporate category.

In January 2015, the company obtained regulatory approval for moving its two U.S. broker-dealers – E*TRADE Clearing LLC and E*TRADE Securities LLC – from under E*TRADE Bank. E*TRADE Securities and E*TRADE Clearing were moved from under E*TRADE Bank in February 2015 and July 2015, respectively. The reorganized structure will aid in simplification of distribution of capital generated by those entities to the parent.

In April 2018, E*TRADE completed the Trust Company of America (TCA) acquisition deal, diversifying business and securing access to high growth Advisor service delivery model. Previously, in an effort to fortify its derivatives platform, the company completed the acquisition of online options broker — OptionsHouse — in September 2016.



▲ E*TRADE, with the introduction of brokerage products and services and enhancement of capabilities on professional trading and mobile platforms, is focused on improving its technology space to offer a better digital experience to customers. The company's DARTs recorded a four-year compound annual growth rate (CAGR) of 21% in 2019, with the increasing trend continued in the first half of 2020. Notably, first-quarter 2020 marked the record total DARTs nearly double the previous peak, while derivative DARTs were more than 65% above the prior record as market volatility achieved new heights amid the coronavirus pandemic-related uncertainties.

E*TRADE remains well positioned for growth due to its online innovations and renewed focus on trading business. Further, strategic moves and steady capital-deployment activities are commendable.

- Zacks Equity Research:
- ETFC**

Reasons To Sell:

- ▼ E*TRADE's expanding cost base exposes the company to operational risks. Notably, non-interest expenses recorded a CAGR of 8.9% over the last four years (2015-2019), primarily due to rise in almost all the cost components. The uptrend continued in the first half of 2020 as well. Therefore, mounting expenses will likely be a near-time headwind as the company focuses on growing its franchise.
 - ▼ E*TRADE has to compete with many established and renowned players with greater financial, marketing and technical capabilities. Some of these competitors are in position to withstand the changing market conditions in a better way and can mould to take advantages of the opportunities. Also, these big peers can easily come out with better terms, conduct promotional activities and can offer better terms to entice customers. This intense competition can have adverse impact on the company's revenues and customer base.
 - ▼ We remain apprehensive about E*TRADE's significant dependence on interest-based revenue streams (net interest income constituted 55% of net revenues in the first half of 2020). Therefore, following the recent moves of Fed on rate cuts, the top line will likely be impacted.
 - ▼ The stock seems overvalued when compared with the broader industry. Its price-earnings (F1) and price-to-book value ratios are above the respective industry averages.
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Escalating expenses and significant dependence on interest-based revenue streams remain key concerns for E*TRADE. Further, intense competition with other established companies keeps us apprehensive.

Recent News

E*TRADE Financial's July DARTs Solid, New Accounts Up Y/Y – Aug 14, 2020

E*TRADE has reported a rise in DARTs for July. According to its monthly-market activity, the company's DARTs came in at 1,014,000, down 27.2% from the previous month but more than 200% up on a year-over-year basis. Notably, derivatives comprised 27% of DARTs in the reported month.

E*TRADE's Shareholders Approve Merger With Morgan Stanley – Jul 17, 2020

Shareholders of E*TRADE have approved the merger agreement with Morgan Stanley. In the meeting, more than 99% of votes were cast in favor of the proposal. Completion of the acquisition is subject to additional customary closing conditions, including receipt of the remaining required regulatory approvals. The company expects the acquisition to close in the fourth quarter of 2020.

In February 2020, Morgan Stanley entered into an all-stock acquisition deal with E*TRADE, per which the former will acquire the latter for \$13 billion. Post completion, Morgan Stanley will be well positioned as a leader in the Wealth Management industry across all channels and wealth segments, with significant increase in the scale and breadth of its franchise.

E*TRADE's more-than 5.2-million client accounts and \$360 billion of retail client assets will augment Morgan Stanley's current 3-million client relationships and \$2.7 trillion of client assets. Thus, the combined entity will have client assets worth \$3.1 trillion, 8.2 million retail client relationships and accounts, and 4.6 million stock-plan participants.

Morgan Stanley will be able to serve clients with superior products and services catering the advisor-driven model, combined with E*TRADE's direct-to-consumer and digital processes. Therefore, Morgan Stanley will be transitioned to a more balance-sheet light business mix, with strong and diversified revenue sources.

"E*TRADE represents an extraordinary growth opportunity for our Wealth Management business and a leap forward in our Wealth Management strategy. The combination adds an iconic brand in the direct-to-consumer channel to our leading advisor-driven model, while also creating a premier Workplace Wealth provider for corporations and their employees. E*TRADE's products, innovation in technology, and established brand will help position Morgan Stanley as a top player across all three channels: Financial Advisory, Self-Directed, and Workplace," said James Gorman, chairman and CEO of Morgan Stanley. "In addition, this continues the decade-long transition of our Firm to a more balance sheet light business mix, emphasizing more durable sources of revenue," Gorman further noted on this.

However, the deal awaits certain regulatory approvals and customary approvals by shareholders of E*TRADE. The transaction is anticipated to close in the final quarter of 2020.

Terms of the Deal

Per terms of the deal, each common shareholder of E*TRADE will get stock equivalent to 1.0432 of Morgan Stanley shares for every E*TRADE share held. This represents per share value of \$58.74 based on the closing price of Morgan Stanley common stock as on Feb 19, 2020.

Strategically, the combined entity will enhance through advanced technologies, innovative products and create a competitive edge with financial stability. Remarkably, on completion of the acquisition, online brokerage and digital banking services will enhance clients' experience.

Mike Pizzi, CEO of E*TRADE, will join Morgan Stanley, looking after the E*TRADE business within Morgan Stanley and head the ongoing integration process. Moreover, one of E*TRADE's independent directors is likely to join Morgan Stanley's board.

Financial Benefits

Catering huge funding benefits to Morgan Stanley, the deal comes with around \$56 billion of low-cost deposits. The acquisition move follows the bank's efforts to record revenues from balance-sheet light and more lasting sources of revenues. Notably, post integration, the combined wealth and investment management businesses are likely to contribute about 57% of the bank's pre-tax profits, excluding potential synergies, above the 26% recorded in 2010.

Post combination, significant cost savings worth \$400 million is expected with optimization of technology infrastructure and shared corporate services, along with funding synergies of \$150 million from E*TRADE's around \$56 billion of deposits. In addition, \$7.3 trillion of combined current customer assets is likely to generate significant revenue opportunities.

Per Morgan Stanley, the acquisition is likely to be accretive once fully phased-in estimated cost and funding synergies are realized. Furthermore, the bank's common equity tier 1 ratio is estimated to expand by more than 30 basis points (bps) on closure and augment the bank's return on tangible common equity by more than 100 bps, with fully phased-in cost and funding synergies. Apart from this, Wealth Management's pre-tax profit margin is expected to be up more than 30%.

Dividend Update

On Jul 23, E*TRADE's board of directors announced a quarterly common stock cash dividend of 14 cents per share. The dividend will be paid on Aug 25, to shareholders on record as of Aug 19, 2020.

Valuation

E*TRADE's shares are up 17.6% in the year-to-date period and 28.6% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 8.2% and 15.5% in the year-to-date period. Over the past year, the Zacks sub-industry is up 9.8% while the sector is down 6.7%.

Top Peers



Company (Ticker)	Rec	Rank
TD Ameritrade Holding Corporation (AMTD)	Outperform	1
Evercore Inc (EVR)	Neutral	3
Interactive Brokers Group, Inc. (IBKR)	Neutral	2
LPL Financial Holdings Inc. (LPLA)	Neutral	3
Raymond James Financial, Inc. (RJF)	Neutral	4
The Charles Schwab Corporation (SCHW)	Neutral	3
Virtu Financial, Inc. (VIRT)	Neutral	3
WisdomTree Investments, Inc. (WETF)	Neutral	3

Industry Comparison Industry: Financial - Investment Bank				Industry Peers		
	ETFC	X Industry	S&P 500	AMTD	RJF	SCHW
Zacks Recommendation (Long Term)	Neutral	-	-	Outperform	Neutral	Neutral
Zacks Rank (Short Term)	2	-	-	1	4	3
VGM Score	F	-	-	F	C	F
Market Cap	11.80 B	929.51 M	23.75 B	20.28 B	10.32 B	44.61 B
# of Analysts	3	2	14	7	2	7
Dividend Yield	1.05%	0.00%	1.62%	3.31%	1.97%	2.08%
Value Score	D	-	-	F	C	F
Cash/Price	0.50	0.71	0.07	1.02	0.90	1.48
EV/EBITDA	4.78	2.45	13.49	0.93	2.45	-1.48
PEG Ratio	1.60	1.12	3.03	NA	NA	NA
Price/Book (P/B)	1.92	1.74	3.18	2.12	1.47	1.74
Price/Cash Flow (P/CF)	10.68	8.93	12.85	7.99	8.93	9.72
P/E (F1)	17.50	13.62	22.17	10.46	13.76	16.18
Price/Sales (P/S)	4.11	1.46	2.49	3.43	1.27	4.30
Earnings Yield	5.71%	7.27%	4.32%	9.55%	7.27%	6.18%
Debt/Equity	0.23	0.39	0.77	0.39	0.47	0.33
Cash Flow (\$/share)	5.00	2.30	6.94	4.69	8.43	3.56
Growth Score	F	-	-	F	D	F
Hist. EPS Growth (3-5 yrs)	34.95%	20.42%	10.44%	30.77%	20.42%	28.06%
Proj. EPS Growth (F1/F0)	-24.32%	-13.45%	-5.97%	-13.25%	-26.08%	-21.32%
Curr. Cash Flow Growth	-5.88%	-0.49%	5.22%	17.86%	13.40%	9.66%
Hist. Cash Flow Growth (3-5 yrs)	13.09%	12.22%	8.52%	21.50%	17.54%	22.65%
Current Ratio	0.30	1.23	1.33	1.11	1.03	0.30
Debt/Capital	17.15%	27.82%	44.59%	28.08%	32.18%	21.67%
Net Margin	28.69%	9.74%	10.13%	32.88%	10.75%	31.48%
Return on Equity	14.59%	12.32%	14.51%	22.51%	13.04%	15.86%
Sales/Assets	0.04	0.19	0.51	0.12	0.19	0.03
Proj. Sales Growth (F1/F0)	-6.43%	0.00%	-1.67%	-4.45%	1.18%	-6.13%
Momentum Score	C	-	-	B	A	D
Daily Price Chg	-1.82%	-0.22%	-0.02%	-1.23%	-0.97%	-1.23%
1 Week Price Chg	3.72%	0.76%	1.09%	3.01%	1.60%	2.97%
4 Week Price Chg	-0.34%	0.85%	4.83%	2.45%	7.01%	2.31%
12 Week Price Chg	29.67%	14.12%	13.09%	10.02%	15.38%	5.45%
52 Week Price Chg	28.57%	-1.86%	2.77%	-14.40%	-2.20%	-8.17%
20 Day Average Volume	1,753,159	79,334	1,932,479	2,490,613	645,718	8,666,214
(F1) EPS Est 1 week change	0.55%	0.00%	0.00%	0.24%	0.00%	0.00%
(F1) EPS Est 4 week change	6.85%	6.85%	1.80%	14.52%	7.05%	-2.16%
(F1) EPS Est 12 week change	9.26%	22.36%	2.88%	22.28%	20.22%	2.60%
(Q1) EPS Est Mthly Chg	14.84%	1.83%	0.80%	28.61%	5.05%	-5.21%

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	D
Growth Score	F
Momentum Score	C
VGM Score	F

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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