

Northern Trust Corp (NTRS)

\$80.89 (As of 03/05/20)

Price Target (6-12 Months): **\$85.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 08/09/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: C

Growth: C

Momentum: D

Summary

Shares of Northern Trust have underperformed the industry in the past three months. Yet, the company has an impressive earnings surprise history, having surpassed the Zacks Consensus Estimate in three of the trailing four quarters. The company continues to gain from strong wealth management operations and diversified products. Implementation of the Target2-Securities strategy to improve client experience bodes well for long-term growth. Steady capital-deployment activities boost shareholders' confidence. Yet, despite undertaking cost-saving measures, mounting expenses due to investments in technology and personnel costs, continue to hurt financials. Declining loan balances puts the top line under pressure. Recently, Northern Trust decreased its prime lending rate from 4.75% to 4.25%, following 50 basis points rate cut by the Federal Reserve.

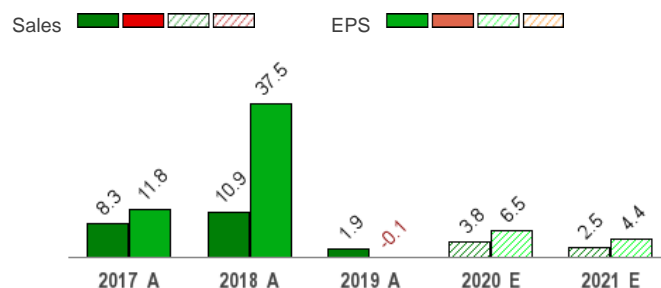
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$110.46 - \$76.80
20 Day Average Volume (sh)	1,515,955
Market Cap	\$16.9 B
YTD Price Change	-23.9%
Beta	1.24
Dividend / Div Yld	\$2.80 / 3.5%
Industry	Banks - Major Regional
Zacks Industry Rank	Top 18% (46 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-4.0%
Last Sales Surprise	0.3%
EPS F1 Est- 4 week change	-0.8%
Expected Report Date	04/28/2020
Earnings ESP	-5.2%
P/E TTM	12.2
P/E F1	11.5
PEG F1	1.2
P/S TTM	2.5

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,632 E	1,659 E	1,672 E	1,694 E	6,461 E
2020	1,569 E	1,583 E	1,593 E	1,608 E	6,301 E
2019	1,481 A	1,507 A	1,538 A	1,548 A	6,073 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.67 E	\$1.95 E	\$1.87 E	\$1.99 E	\$7.37 E
2020	\$1.56 E	\$1.81 E	\$1.75 E	\$1.85 E	\$7.06 E
2019	\$1.48 A	\$1.75 A	\$1.69 A	\$1.70 A	\$6.63 A

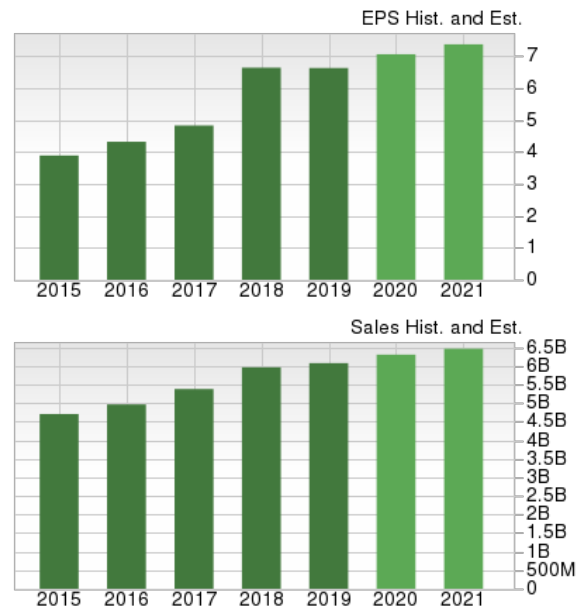
*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/05/2020. The reports text is as of 03/06/2020.

Overview

Northern Trust Corporation is the holding company for its main subsidiary, Northern Trust Company, as well as a number of other banking and non-banking financial service subsidiaries. The company's main sources of revenue include two of its primary business units: Corporate and Institutional Services (C&IS) and Wealth Management (WM). Asset management and related services to WM and C&IS clients are provided primarily by a third business unit, Asset Management.

- The C&IS unit (accounted for 57% of 2019 total fees) provides asset servicing, asset management and related services to clients including corporate and public retirement funds, foundations and government funds; commercial banking services to large and mid-sized corporations and financial institutions; and foreign exchange services. As of Dec 31, 2019, total C&IS assets under custody (AUC) were \$8.5 trillion and assets under management (AUM) were \$917.5 billion.
- The WM division (43%) delivers customized investment management and trust services to high net worth individuals and families across 18 states of North America and Washington, D.C., as well as offices in London and Guernsey. As of Dec 31, 2019, total AUC was \$735.7 billion and total AUM was \$313.8 billion.
- Asset Management provides a broad range of asset management and related services and other products to clients around the world, including clients of C&IS and WM.



Treasury and Other includes income and expense related to the wholesale funding activities and the investment portfolios of the Corporation and the Bank and nonrecurring items not allocated to C&IS and WM.

In November 2018, Northern Trust acquired Chicago-based BEx LLC — a foreign exchange software solutions provider — for \$37.6 million to strengthen its Global Foreign Exchange business. In June 2018, Northern Trust completed the acquisition of Citadel's Omnium Technology Platform. In October 2017, Northern Trust acquired UBS Asset Management's fund administration servicing units in Luxembourg and Switzerland.

As of Dec 31, 2019, the company had total assets worth \$136.83 billion, AUM of \$1.23 trillion and AUC of \$9.23 trillion.



Reasons To Buy:

- ▲ Against the backdrop of macroeconomic headwinds, Northern Trust, with heightened aggression was focused on initiating new business over the last few years. Additionally, Northern Trust's innovative technology-driven hedge fund administration capabilities brought to the marketplace via Northern Trust Hedge Fund Services clearly provides an attractive proposition to the clients. Further, implementation of the Target2-Securities (T2S) strategy to provide better services to its clients is commendable.
- ▲ Northern Trust displayed its capital strength as it successfully cleared the 2019 Dodd-Frank Act Stress Test (DFAST). Following this, the company increased its quarterly common stock dividend to 70 cents per share, effective third-quarter 2019. The plan also includes repurchase up to \$1.4 billion of common stock between July 2019 and June 2020. Notably, the company's debt/equity ratio compares favorably with that of the broader industry, highlighting the fact that such dividend hikes are sustainable in the future.
- ▲ Organic growth remains a key strength at Northern Trust, as reflected by its revenue growth story. Revenues witnessed a CAGR of 6.6% over the last five years (2015–2019) on rising net interest as well as non-interest income. We believe the company is well positioned to maintain this trend in the days to come.
- ▲ Northern Trust benefited from the rise in interest rates in the past few years. In 2016, 2017, 2018 and 2019, the net interest margin improved on a year-over-year basis, despite three rate cuts in 2019. Also, a continued rise in yields on earning assets provided support. Therefore, margin is likely to expand in the quarters ahead, given a decent lending scenario. Recently, Northern Trust decreased its prime lending rate from 4.75% to 4.25%, following 50 basis points rate cut by the Federal Reserve.
- ▲ For supporting the new investment activities, management is taking steps to tackle expense growth and reinstate operating leverage over the upcoming quarters. Northern Trust continues to pursue meaningful additional efforts to improve productivity and deliver financial benefits beyond original targets. In 2014, the company established internal productivity targets on both the revenue and expense side. The ultimate measure of the success of these efforts was the company's ability to consistently achieve its financial target of a return on equity between 10% and 15%. Notably, the company recorded ROE of 14.9% as of Dec 31, 2019. Further, through Value for Spend initiative, which was started in 2017, the company has realigning the expense base with the goal of realizing \$250 million in expense run rate savings by 2020.
- ▲ Though there was a sequential uptick in the third quarter of 2012, credit quality improved and continued to move toward a normalized level in 2013 and thereafter. Notably, provision for credit losses remained low in 2014, driven by an improvement in commercial and institutional along with commercial and residential real estate loans. Further, provisions recorded a benefit in the last five years (ended 2019). We believe, with the continuation of such a favorable trend in the future, the company will be able to strengthen its earnings.

Northern Trust remains focused on initiating new business to tackle macroeconomic headwinds. Rising revenues bolster organic growth, while no provisions boosts the company's bottom line growth.

Reasons To Sell:

- ▼ Despite successful implementation of expense reduction initiatives, costs escalated on ongoing investments in technology driving compensation and equipment and software expenses. Notably, non-interest expenses witnessed a CAGR of 6% over the last five years (2015–2019). We believe an increasing trend in expenses will remain a hindrance for bottom-line growth. Notably, management targets the goal of realizing \$250 million in expense run-rate savings by 2020.
- ▼ Northern Trust's loan balances have been witnessing a declining trend, which keeps its interest income under pressure. In the last four years (ended 2019), loans and leases witnessed a negative CAGR of 2.4%. The company has been recording decline majorly in the commercial and industrial, along with commercial and residential real estate loans due to lack of confidence and uncertainties related to trade war and global economic slowdown prevailing in the markets. Therefore, continuation of such trend might impact top-line expansion of the company.
- ▼ Northern Trust runs a global business. Changing conditions of the global financial markets and general economic conditions could adversely affect the company's businesses. Weak economic conditions had affected wealth creation, investment preferences, trading activities, and savings patterns, which in turn impacted demand for trust and investment products and services. Though equity markets started to improve, in the absence of a sustained recovery, reduction in transaction volumes might negatively affect earnings in the coming quarters.
- ▼ Shares of Northern Trust have underperformed the industry in the past three months. With this unfavorable trend, the company's current-year earnings estimates have been revised slightly downward over the past 30 days. Also, the stock seems overvalued when compared with the broader industry. Its current price-to-book (P/B) and price-earnings (P/E) (F1) ratios are above the respective industry averages. Therefore, given the above concerns and lack of positive estimate revisions, the stock has limited upside potential.

Rising expenses on account of investments in technology and declining loans balance remain key headwinds for Northern Trust. Also, stretched valuation indicates limited upside potential in the stock.

Last Earnings Report

Northern Trust Q4 Earnings Miss Estimates on High Costs

Northern Trust reported a negative earnings surprise of 4% in fourth-quarter 2019. Earnings per share of \$1.70 lagged the Zacks Consensus Estimate of \$1.77. Moreover, the reported figure declined 5.6% year over year. Results included certain one-time items.

Escalating operating expenses was on the downside during the quarter. However, higher revenues, aided by rise in fee income, were a driving factor. Also, net interest margin escalated. Moreover, most credit metrics marked significant improvements.

Net income came in at \$371.1 million, down 9% year over year.

For full-year 2019, net income was \$1.5 billion or \$6.63 per share compared with the prior year's \$1.6 billion or \$6.64 per share. The Zacks Consensus Estimate was pinned at \$7.29.

Margins & Revenues Improve, Costs Escalate

For full-year 2019, revenues on a fully taxable equivalent basis, were \$6.1 billion, up 1.7% from the \$6 billion reported in 2018. However, the figure lagged the Zacks Consensus Estimate of \$6.3 billion.

Total revenues of \$1.56 billion improved 3% year over year in the quarter. Further, the revenue figure surpassed the Zacks Consensus Estimate of \$1.54 billion.

On a fully-taxable equivalent basis, net interest income of \$430.5 million was almost stable year on year.

Net interest margin (NIM) was 1.59%, up 7 basis points from the prior-year quarter. The upside chiefly reflects the impact of reduced foreign-exchange swap volume and a balance-sheet mix shift, partly mitigated by lower short-term interest rates.

Consolidated Trust, Investment and Other Servicing Fees summed \$992.2 million, up 6% year over year.

Non-interest income escalated 4% from the year-ago quarter to \$1.12 billion. Rise in trust, investment and other servicing fees, along with security commissions and trading income, led to this upsurge. These increases were partly offset by lower foreign-exchange trading income, treasury management fees and other operating income.

Non-interest expenses flared up 5% year over year to \$1.07 billion during the October-December period. This upswing mainly resulted from an elevation in compensation, employee benefits, occupancy, outside services, equipment and software expenses. These were partly negated by lower other expenses.

Assets Under Management and Custody Climb

As of Dec 31, 2019, Northern Trust's total assets under custody climbed 22% year over year to \$9.2 trillion, while total assets under management increased 15% to \$1.2 trillion.

Credit Quality: A Marked Improvement

Total allowance for credit losses came in at \$124.4 million, down 10% year over year. Net charge offs were \$2.3 million compared with the net recoveries of \$1.7 million reported in the year-ago quarter.

Further, non-performing assets decreased 26.3% year over year to \$86.8 million as of Dec 31, 2019. Credit provision was \$1 million in the quarter compared with the \$4 million of credit provision reported in the prior-year quarter.

Strong Capital Position

Under the Advanced Approach, as of Dec 31, 2019, Tier 1 capital ratio, total capital ratio and Tier 1 leverage ratio came in at 15.2%, 16.9% and 8.7%, compared with 15%, 16.9% and 8%, respectively, witnessed in the prior-year quarter. All ratios exceeded the regulatory requirements.

Return on average common equity was 14.8% compared with the year-earlier quarter's 17%. Return on average assets was 1.25% compared with the 1.34% witnessed in the year-ago quarter.

Capital Deployment Update

During 2019, Northern Trust repurchased 11.78 million shares for \$1.1 billion at an average price of \$93.40 per share. Notably, during the reported quarter, the company repurchased 2.61 million shares for \$264.4 million, at an average price of \$101.33 per share. This includes shares related to share-based compensation.

Outlook

During fourth-quarter 2019, the company added to its bank-owned life insurance program that was first put in place during the second quarter. The full quarterly run rate is likely to reach in the first quarter of 2020, with an additional net interest income decline of around \$2.3 million and

Quarter Ending 12/2019

Report Date	Jan 22, 2020
Sales Surprise	0.29%
EPS Surprise	-3.95%
Quarterly EPS	1.70
Annual EPS (TTM)	6.62

other operating income increase of \$2.7 million on a sequential basis.

Related to benefits expense in 2020, due to changes in underlying assumptions, management expects to record an increase in full-year pension expense of just more than \$30 million, which represents a 0.7% increase in overall total 2019 expense base.

Recent News

Northern Trust Decreases its Prime Lending Rate by 25 Bps - Mar 4, 2020

Pursuant to the U.S. Federal Reserve's interest rate cut by 50 bps, Northern Trust reduced its prime lending rate from 4.75% to 4.25%, effective Mar 4. Prior to this, the company reduced the rate to 4.75% in October 2019.

Dividend Update

On Jan 21, Northern Trust announced a quarterly common stock dividend of 70 cents per share on its common stock. The dividend will be paid on Apr 1 to shareholders of record as of Mar 13, 2020.

Valuation

Northern Trust's shares are down 23.9% in the year-to-date period and 10.1% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 17.9% and 7.7%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry and the sector is up 0.3% and 1.7%, respectively.

The S&P 500 Index is down 3% in the year-to-date period while up 12.5% in the past year.

The stock is currently trading at 11.25X forward 12 months earnings, which compares to 9.78X for the Zacks sub-industry, 13.74X for the Zacks sector and 17.88X for the S&P 500 index.

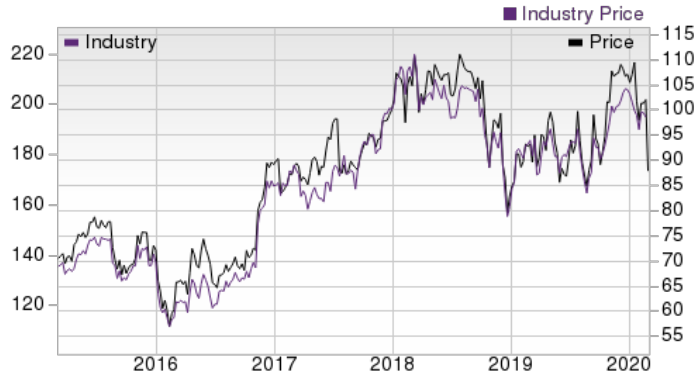
Over the past five years, the stock has traded as high as 21.62X and as low as 11.08X, with a 5-year median of 16X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$85 price target reflects 11.82X forward earnings.

The table below shows summary valuation data for NTRS

Valuation Multiples - NTRS					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	11.25	9.78	13.74	17.88
	5-Year High	21.62	13.85	16.21	19.34
	5-Year Low	11.08	9.04	12.01	15.18
	5-Year Median	16	11.36	13.97	17.46
P/TB TTM	Current	1.88	1.95	2.91	11.93
	5-Year High	2.89	2.68	3.98	12.94
	5-Year Low	1.63	1.44	2.44	6.03
	5-Year Median	2.31	2.12	3.46	9.13
P/S F12M	Current	2.66	3.28	6.55	3.3
	5-Year High	4.29	4.59	6.65	3.43
	5-Year Low	2.54	2.61	5.39	2.54
	5-Year Median	3.55	3.59	6.04	3.01

As of 03/05/2020

Industry Analysis Zacks Industry Rank: Top 18% (46 out of 255)



Top Peers

JPMorgan Chase & Co. (JPM)	Outperform
M&T Bank Corporation (MTB)	Outperform
State Street Corporation (STT)	Outperform
The Bank of New York Mellon Corporation (BK)	Neutral
Citigroup Inc. (C)	Neutral
First Republic Bank (FRC)	Neutral
U.S. Bancorp (USB)	Neutral
HSBC Holdings plc (HSBC)	Underperform

Industry Comparison Industry: Banks - Major Regional				Industry Peers		
	NTRS Neutral	X Industry	S&P 500	BK Neutral	MTB Outperform	STT Outperform
VGM Score	D	-	-	F	D	D
Market Cap	16.93 B	33.42 B	21.47 B	34.78 B	17.16 B	22.11 B
# of Analysts	7	8	13	8	8	8
Dividend Yield	3.46%	3.46%	2.04%	3.16%	3.34%	3.33%
Value Score	C	-	-	D	B	B
Cash/Price	2.39	0.80	0.05	4.46	0.50	3.09
EV/EBITDA	-7.76	4.26	12.81	-9.52	5.24	-7.79
PEG Ratio	1.14	1.19	1.88	1.24	1.60	0.83
Price/Book (P/B)	1.75	1.00	2.95	0.95	1.20	1.06
Price/Cash Flow (P/CF)	8.50	7.36	11.75	6.85	7.79	5.85
P/E (F1)	11.18	9.51	17.19	9.52	9.45	9.10
Price/Sales (P/S)	2.45	2.01	2.32	1.67	2.47	1.68
Earnings Yield	8.73%	10.52%	5.81%	10.51%	10.59%	10.99%
Debt/Equity	0.41	0.86	0.70	0.74	0.48	0.58
Cash Flow (\$/share)	9.51	6.63	7.01	5.74	16.90	10.66
Growth Score	C	-	-	F	F	D
Hist. EPS Growth (3-5 yrs)	16.37%	13.58%	10.85%	11.50%	17.92%	7.88%
Proj. EPS Growth (F1/F0)	6.51%	4.50%	6.27%	2.67%	1.32%	11.16%
Curr. Cash Flow Growth	-5.52%	2.66%	6.07%	-5.62%	5.45%	-5.72%
Hist. Cash Flow Growth (3-5 yrs)	10.90%	7.71%	8.52%	5.07%	11.65%	5.53%
Current Ratio	0.65	0.90	1.23	0.70	1.08	0.50
Debt/Capital	26.50%	43.35%	42.57%	40.45%	30.77%	33.86%
Net Margin	21.64%	22.06%	11.69%	21.39%	27.79%	18.14%
Return on Equity	15.15%	11.95%	16.66%	10.49%	13.37%	11.81%
Sales/Assets	0.05	0.05	0.54	0.06	0.06	0.05
Proj. Sales Growth (F1/F0)	3.75%	0.41%	3.90%	-3.94%	-2.40%	-0.24%
Momentum Score	D	-	-	D	D	F
Daily Price Chg	-4.89%	-5.92%	-3.79%	-2.96%	-8.04%	-6.87%
1 Week Price Chg	-13.91%	-15.75%	-12.06%	-11.41%	-16.72%	-11.69%
4 Week Price Chg	-21.20%	-20.11%	-10.92%	-17.33%	-23.11%	-22.26%
12 Week Price Chg	-26.38%	-23.27%	-8.10%	-23.27%	-23.49%	-22.41%
52 Week Price Chg	-10.10%	-10.98%	4.09%	-23.29%	-21.50%	-8.75%
20 Day Average Volume	1,515,955	6,079,369	2,483,920	6,320,289	870,424	3,107,334
(F1) EPS Est 1 week change	-0.96%	-0.37%	0.00%	-0.72%	-0.52%	-0.97%
(F1) EPS Est 4 week change	-0.84%	-0.41%	-0.06%	-0.36%	-0.52%	-0.58%
(F1) EPS Est 12 week change	-1.02%	0.60%	-0.42%	-2.31%	4.00%	6.77%
(Q1) EPS Est Mthly Chg	-1.47%	-0.20%	-0.29%	-0.42%	-0.16%	-0.97%

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	C
Growth Score	C
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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