

Northern Trust Corp (NTRS)

\$74.77 (As of 05/11/20)

Price Target (6-12 Months): **\$63.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 03/13/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:F

Value: F

Growth: F

Momentum: B

Summary

Shares of Northern Trust have outperformed the industry in the past three months. Also, the company has an impressive earnings surprise history, having surpassed the Zacks Consensus Estimate in three of the trailing four quarters. The first-quarter 2020 results reflected higher revenues, margin pressure along with elevated costs and provisions. The company continues to gain from strong wealth-management operations and diversified products along with implementation of the Target2-Securities strategy. Nevertheless, despite undertaking cost-saving measures, mounting expenses due to investments in technology and personnel costs, keep dampening financials. Decline in loan balances puts the top line under pressure. Notably, the company has suspended its share buybacks with an aim to use the capital for lending activities amid the coronavirus pandemic.

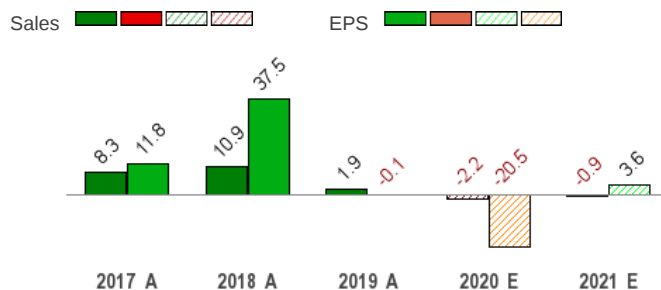
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$110.46 - \$60.67
20 Day Average Volume (sh)	1,406,565
Market Cap	\$15.6 B
YTD Price Change	-29.6%
Beta	1.09
Dividend / Div Yld	\$2.80 / 3.7%
Industry	Banks - Major Regional
Zacks Industry Rank	Bottom 5% (240 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	6.9%
Last Sales Surprise	3.2%
EPS F1 Est- 4 week change	2.3%
Expected Report Date	07/22/2020
Earnings ESP	0.0%
P/E TTM	11.2
P/E F1	14.2
PEG F1	1.5
P/S TTM	2.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,513 E	1,544 E	1,552 E	1,572 E	5,886 E
2020	1,588 A	1,452 E	1,428 E	1,435 E	5,942 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	\$1.28 E	\$1.50 E	\$1.39 E	\$1.47 E	\$5.46 E
2020	\$1.55 A	\$1.28 E	\$1.24 E	\$1.37 E	\$5.27 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 05/11/2020. The reports text is as of 05/12/2020.

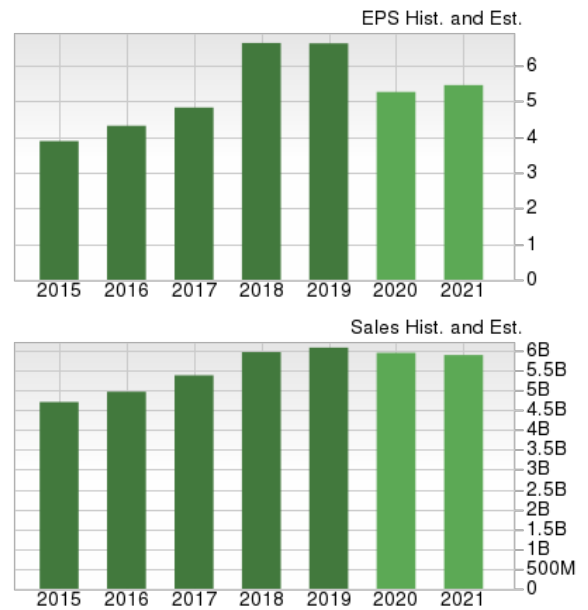
Overview

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 Asset Management business.

- 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 Mar 31, 2020, total C&IS assets under custody (AUC) were \$7.6 trillion and assets under management (AUM) were \$842.6 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 Mar 31, 2020, total AUC was \$633.9 billion and total AUM was \$276.7 billion.
- 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 Mar 31, 2020, the company had total assets worth \$161.7 billion, AUM of \$1.12 trillion and AUC of \$8.25 trillion.



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), with the increasing trend continued in first-quarter 2020. We believe an increasing trend in expenses will remain a hindrance for bottom-line growth. Notably, management exceeded the goal of realizing \$250 million in expense run-rate savings in the first quarter.
- ▼ Northern Trust's loan balances have been witnessing a declining trend, which keeps its interest income under pressure. Though loans and leases escalated in the first-quarter 2020 on rising commercial and institutional, private client, and commercial real estate loans, in the last four years (ended 2019), it witnessed a negative CAGR of 2.4%. The company has recorded declines, 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, further decline in loans might impact its top-line expansion.
- ▼ 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. Amid volatile equity markets and in the absence of a sustained recovery, reduction in transaction volumes might affect earnings in the coming quarters.
- ▼ Shares of Northern Trust have outperformed the industry in the past three months. Despite this favorable trend, the company's current-year earnings estimates have been revised 22.6% downward over the past 60 days. Also, the stock seems overvalued when compared with the broader industry. Its current price-to-book (P/B) and price-to-sales 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.

Risks

- 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. However, the company has temporarily suspended share buybacks through the second quarter, following the "unprecedented challenge" from the coronavirus pandemic.
 - 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 non-interest income, with the trend continuing in first-quarter 2020. 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. Though margin declined in first-quarter 2020 on low rates, the same is likely to expand in the quarters ahead, given a decent lending scenario.
 - Amid the coronavirus crisis and its impact on economy, the company holds a debt level of \$11.8 billion and debt-capital ratio of 0.28 (compared with the industry average of 0.5), as of Mar 31, 2020. Both has been increasing over the past few quarters. Nevertheless, with a time-interest-earned of 7.5X which indicates the company's ability to meet its debt obligations based on current income, we believe Northern Trust carries lower credit risk, and a lesser likelihood of default of interest and debt repayments if the economic situation worsens.
 - 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 13.4% as of Mar 31, 2020. 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. Though provisions escalated in first-quarter 2020 on coronavirus concerns, it 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.
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Last Earnings Report

Northern Trust Q1 Earnings Beat Estimates, Provisions Escalate

Northern Trust delivered first-quarter 2020 earnings per share of \$1.55, surpassing the Zacks Consensus Estimate of \$1.45, riding on higher fee income. Also, the reported figure climbed 5% year over year.

Higher revenues, aided by a rise in fee income, were a driving factor. However, decline in net interest margin was on the downside. Moreover, escalating operating expenses and provisions were major drags.

Net income came in at \$360.6 million, up 4% year over year.

Revenues Improve, Costs Escalate

Total revenues of \$1.6 billion improved 7% year over year in the first quarter. Further, the revenue figure beat the Zacks Consensus Estimate of \$1.54 billion.

On a fully-taxable equivalent basis, net interest income of \$416.2 million declined 3% year on year, mainly on lower net interest margin.

NIM was 1.51%, down 7 basis points from the prior-year quarter. This decline chiefly reflects the impact of lower short-term interest rates, partly muted by a balance-sheet mix shift.

Consolidated Trust, Investment and Other Servicing Fees summed \$1 billion, up 8% year over year.

Non-interest income climbed 11% from the year-ago quarter to \$1.18 billion. Rise in trust, investment and other servicing fees, foreign-exchange trading income, along with security commissions and trading income and other operating income, led to this upsurge. These increases were partly offset by lower treasury management fees.

Non-interest expenses flared up 4% year over year to \$1.07 billion during the January-March period. This upswing mainly resulted from an elevation in compensation, employee benefits, outside services, equipment and software expenses. These were partly negated by lower occupancy and other expenses.

Assets Under Management and Custody

As of Mar 31, 2020, Northern Trust's total assets under custody inched up 1% year over year to \$8.3 trillion, while total assets under management decreased 4% to \$1.1 trillion.

Credit Quality: A Mixed bag

Total allowance for credit losses came in at \$198.4 million, up 42% year over year. Net charge offs were \$0.7 million compared with the net recoveries of \$1.2 million reported in the year-ago quarter.

Provision for credit losses was \$61 million in the quarter compared with the nil provision reported in the prior-year quarter. Notably, provisions flared up on the coronavirus crisis. However, non-accrual assets decreased 15% year over year to \$105.5 million as of Mar 31, 2020.

Strong Capital Position

Under the Advanced Approach, as of Mar 31, 2020, Tier 1 capital ratio, total capital ratio and Tier 1 leverage ratio came in at 14.1%, 15.7% and 8.1%, compared with the 14.8%, 16.6% and 8.2%, respectively, witnessed in the prior-year quarter. All ratios exceeded the regulatory requirements.

Return on average common equity was 13.4% compared with the year-earlier quarter's 14%. Return on average assets was 1.17% compared with the 1.18% witnessed in the year-ago quarter.

Capital Deployment Update

During the reported quarter, the company repurchased 3.24 million shares for \$296.8 million, at an average price of \$91.59 per share. This includes shares related to share-based compensation.

Outlook

Looking ahead to the remainder of the year, management expects the macroeconomic environment to certainly create headwinds for certain revenue lines. Firstly, it relates to lower expenses. Further, pressure on net interest margin and net interest income is expected through the year. Management expects NII to decline 7-10% on a sequential basis in the second quarter.

While month lag and quarter lag equity markets were mainly favorable for the first quarter, management expects an impact on the fees. Period end assets under custody/administration and assets under management are expected to decline sequentially by 10% and 9%, respectively. Moreover, the three quarters are also sensitive to asset level.

If economic conditions continue to worsen over the course of the year, management expects to recognize additional provisions.

Quarter Ending 03/2020

Report Date	Apr 21, 2020
Sales Surprise	3.24%
EPS Surprise	6.90%
Quarterly EPS	1.55
Annual EPS (TTM)	6.69

Recent News

Northern Trust Decreases its Prime Lending Rate to 3.25% - Mar 16, 2020

Pursuant to the U.S. Federal Reserve's interest rate cut by 1%, Northern Trust reduced its prime lending rate from 4.25% to 3.25%, effective Mar 16. Prior to this, the company reduced the rate to 4.25% by 50 bps in early March.

Dividend Update

On Apr 21, Northern Trust announced a quarterly common stock dividend of 70 cents per share on its common stock. The dividend will be paid on Jul 1 to shareholders of record as of Jun 12, 2020.

Valuation

Northern Trust's shares are down 29.6% in the year-to-date period and 20.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 40.2% and 26.4%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry and the sector are down 27.2% and 19%, respectively.

The S&P 500 Index is down 9.1% in the year-to-date period but up 3.9% in the past year.

The stock is currently trading at 14.01X forward 12 months earnings, which compares to 12.94X for the Zacks sub-industry, 15.15X for the Zacks sector and 21.15X for the S&P 500 index.

Over the past five years, the stock has traded as high as 21.62X and as low as 9.14X, with a 5-year median of 15.84X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$63 price target reflects 11.8X 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	14.01	12.94	15.15	21.15
	5-Year High	21.62	14.2	16.18	21.15
	5-Year Low	9.14	8.01	11.58	15.19
	5-Year Median	15.84	11.31	13.94	17.45
P/TB TTM	Current	1.69	1.39	2.43	11.54
	5-Year High	2.89	2.68	4	12.78
	5-Year Low	1.45	1.21	1.99	6.02
	5-Year Median	2.31	2.12	3.47	9.22
P/S F12M	Current	2.63	2.53	5.81	3.3
	5-Year High	4.29	4.59	6.7	3.44
	5-Year Low	2.06	2.39	4.99	2.54
	5-Year Median	3.53	3.59	6.05	3.02

As of 05/11/2020

Industry Analysis Zacks Industry Rank: Bottom 5% (240 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
The Bank of New York Mellon Corporation (BK)	Neutral	3
Citigroup Inc (C)	Neutral	3
First Republic Bank (FRC)	Neutral	3
HSBC Holdings plc (HSBC)	Neutral	4
State Street Corporation (STT)	Neutral	3
JPMorgan ChaseCo (JPM)	Underperform	3
MT Bank Corporation (MTB)	Underperform	5
US Bancorp (USB)	Underperform	5

Industry Comparison Industry: Banks - Major Regional				Industry Peers		
	NTRS	X Industry	S&P 500	BK	MTB	STT
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Underperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	5	3
VGM Score	F	-	-	D	F	B
Market Cap	15.56 B	30.50 B	19.55 B	30.50 B	12.74 B	20.68 B
# of Analysts	5	8	14	7	8	7
Dividend Yield	3.74%	4.63%	2.13%	3.60%	4.43%	3.54%
Value Score	F	-	-	D	F	B
Cash/Price	3.60	1.06	0.06	6.86	0.85	7.29
EV/EBITDA	-12.95	2.86	11.85	-15.67	2.86	-24.34
PEG Ratio	1.45	2.09	2.60	1.28	4.50	0.96
Price/Book (P/B)	1.56	0.81	2.71	0.81	0.89	0.97
Price/Cash Flow (P/CF)	7.86	5.88	10.71	6.01	5.88	5.51
P/E (F1)	14.19	14.94	19.55	9.35	12.63	10.27
Price/Sales (P/S)	2.26	1.58	2.01	1.47	1.86	1.58
Earnings Yield	7.05%	6.69%	4.85%	10.68%	7.91%	9.73%
Debt/Equity	0.41	1.06	0.76	0.77	0.43	0.73
Cash Flow (\$/share)	9.51	6.63	7.01	5.74	16.90	10.66
Growth Score	F	-	-	F	F	C
Hist. EPS Growth (3-5 yrs)	16.16%	12.51%	10.82%	10.63%	17.81%	7.98%
Proj. EPS Growth (F1/F0)	-20.54%	-48.67%	-9.99%	-8.39%	-42.80%	-7.29%
Curr. Cash Flow Growth	-5.52%	2.66%	5.83%	-5.62%	5.45%	-5.72%
Hist. Cash Flow Growth (3-5 yrs)	10.90%	9.49%	8.52%	5.07%	11.65%	5.53%
Current Ratio	0.68	0.90	1.27	0.72	1.07	0.59
Debt/Capital	27.57%	49.85%	44.41%	41.44%	28.56%	39.44%
Net Margin	21.88%	21.37%	10.59%	21.60%	24.99%	19.13%
Return on Equity	15.18%	10.59%	16.36%	10.59%	11.84%	12.36%
Sales/Assets	0.05	0.05	0.55	0.05	0.06	0.05
Proj. Sales Growth (F1/F0)	-2.16%	-3.92%	-2.41%	-5.16%	-3.92%	-3.17%
Momentum Score	B	-	-	A	A	A
Daily Price Chg	-1.61%	-4.20%	-0.95%	-2.52%	-5.27%	-2.42%
1 Week Price Chg	0.69%	1.76%	3.23%	-1.83%	-2.17%	1.93%
4 Week Price Chg	-10.51%	-5.60%	4.49%	-4.31%	-10.31%	-1.14%
12 Week Price Chg	-26.12%	-39.49%	-20.09%	-24.95%	-41.49%	-24.52%
52 Week Price Chg	-20.42%	-31.55%	-7.00%	-26.94%	-38.55%	-7.00%
20 Day Average Volume	1,406,565	6,312,961	2,530,553	5,410,508	759,505	2,355,535
(F1) EPS Est 1 week change	-0.04%	0.00%	0.00%	0.47%	0.00%	0.02%
(F1) EPS Est 4 week change	2.32%	-19.32%	-6.07%	8.59%	-0.46%	8.95%
(F1) EPS Est 12 week change	-25.94%	-51.63%	-15.69%	-11.10%	-43.84%	-17.09%
(Q1) EPS Est Mthly Chg	-0.03%	-1.11%	-12.45%	3.88%	13.34%	15.23%

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	F
Growth Score	F
Momentum Score	B
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.

Disclosures

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