

Prosperity Bancshares (PB)

\$48.04 (As of 04/21/20)

Price Target (6-12 Months): **\$54.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/17/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: D

Growth: D

Momentum: C

Summary

Shares of Prosperity Bancshares have outperformed the industry over the past year. Also, the bank has an impressive earnings surprise history, having surpassed the Zacks Consensus Estimate for earnings in three of the trailing four quarters. The acquisition of LegacyTexas Financial will be accretive to the company's earnings in 2020 and also lead to cost savings. Improving asset quality, and solid loan and deposit balances are likely to support profitability. Moreover, steady capital deployment actions reflect strong balance sheet position. However, weakness in mortgage banking business and pressure on margins (due to low interest rates) are likely to have an adverse impact on revenue growth. Also, mounting costs might hamper bottom-line growth. Further, the earnings estimates have been going down ahead of its first quarter 2020 results.

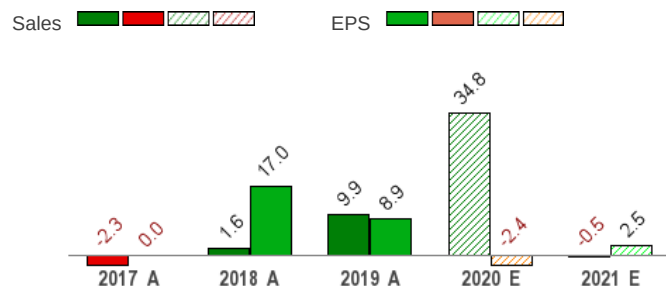
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$75.22 - \$42.02
20 Day Average Volume (sh)	806,971
Market Cap	\$4.6 B
YTD Price Change	-33.2%
Beta	1.36
Dividend / Div Yld	\$1.84 / 3.7%
Industry	Banks - Southwest
Zacks Industry Rank	Bottom 26% (188 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	17.1%
Last Sales Surprise	7.6%
EPS F1 Est- 4 week change	-6.6%
Expected Report Date	04/29/2020
Earnings ESP	0.9%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	268 E	273 E	277 E	279 E	1,100 E
2020	281 E	276 E	277 E	276 E	1,105 E
2019	183 A	185 A	185 A	268 A	820 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.25 E	\$1.29 E	\$1.32 E	\$1.33 E	\$5.02 E
2020	\$1.22 E	\$1.22 E	\$1.31 E	\$1.33 E	\$4.90 E
2019	\$1.18 A	\$1.18 A	\$1.19 A	\$1.44 A	\$5.02 A

*Quarterly figures may not add up to annual.

P/E TTM	9.6
P/E F1	9.8
PEG F1	1.2
P/S TTM	4.8

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/21/2020. The reports text is as of 04/22/2020.

Overview

Houston, TX-based Prosperity Bancshares, Inc. was formed in 1983 as a vehicle to acquire the former Allied Bank in Edna, TX, which was chartered in 1949 as The First National Bank of Edna and is presently known as Prosperity Bank. The financial holding company, pursuant to the Gramm-Leach-Bliley Act, derives substantially all of its revenues and income from its bank subsidiary — Prosperity Bank.

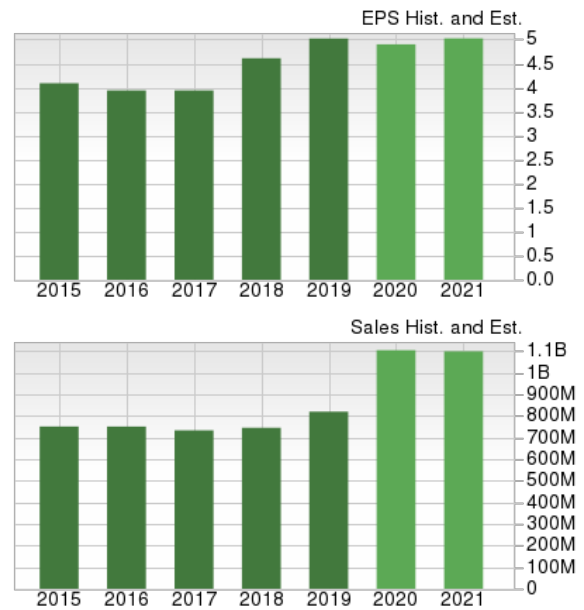
Prosperity Bank provides a wide range of financial products and services — traditional loan and deposit products — to small and medium-sized businesses and consumers. The company provides loans to businesses in the range of \$0.1 million to \$8.0 million. As of Dec 31, 2019, Prosperity Bank operated nearly 240 full-service banking centers.

Since its inception, Prosperity Bancshares has been growing considerably through the acquisition of community banks and branches of other banks. Moreover, since 1998, the company has completed more than 30 deals.

The major buyouts include Commercial Bancshares, Inc. in 2001, First Capital Bankers, Inc. in 2005, Texas United Bancshares, Inc. in 2007, Franklin Bank in 2008 and First Bank in 2010. Further, in 2012, Prosperity Bancshares acquired Texas Bankers, Inc., The Bank Arlington, American State Financial Corporation and Bellaire-based Community National Bank.

In 2013, Prosperity Bancshares completed the buyouts of East Texas Financial Services Inc., Coppermark Bancshares, Inc. and FVNB Corp. In 2014, the company acquired F&M Bancorporation Inc., while in 2016 it completed the merger of Tradition Bancshares, Inc. In 2019, it completed the acquisition of LegacyTexas Financial Group, Inc.

As of Dec 31, 2019, Prosperity Bancshares had total assets of \$32.2 billion, cash and due from banks of \$573.6 million, total loans of \$18.8 billion, total deposits of \$24.2 billion and shareholders' equity of \$6 billion.



Reasons To Buy:

- ▲ Acquisitions remain one of the major contributors to Prosperity Bancshares' growth. Over the years, the company has significantly expanded its operations through the buyout of community banks and branches of other banks. Since 1998, it has completed more than 30 deals. In November 2019, the bank completed the acquisition of LegacyTexas Financial, which will be accretive to its earnings this year. Given the strong balance sheet position, the company is expected to continue similar expansion strategy.
- ▲ Prosperity Bancshares' growth strategy is driven by organic expansion efforts. The company's net revenues witnessed a five-year (2015-2019) CAGR of 2.2%. This upside mainly stemmed from higher loan balances and acquisitions. Further, the company has been able to improve its deposit mix. Non-interest-bearing demand deposits saw a three-year CAGR of 17.5% (ended 2019). Rise in demand for loans will likely continue to aid revenues in the upcoming quarters also.
- ▲ We remain encouraged by Prosperity Bancshares' steady capital deployment activities. The company has been consistently increasing its dividend annually since 1999, with the last hike announced in October 2019. Further, in January, it had announced a share repurchase program (expiring in January 2021) to buy back up to nearly 4.7 million shares. Given the company's strong balance sheet position and zero debt, enhanced capital deployment activities are projected to remain sustainable.
- ▲ Further, Prosperity Bancshares seems undervalued compared with the broader industry. Its current price/book (P/B) and PEG ratios are below the respective industry averages.

Inorganic expansion efforts, higher loan balance and solid balance sheet position will aid Prosperity Bancshares' profits. Further, the bank's capital deployment actions are impressive.

Reasons To Sell:

- ▼ Prosperity Bancshares' net interest margin (NIM) continues to remain under pressure. Though NIM increased to 3.32% in 2019, it has been persistently declining over the past several years — 3.18% in 2018, 3.19% in 2017, 3.35% in 2016, 3.38% in 2015 and 3.80% in 2014. The company's NIM is expected to remain under strain owing to the near-zero interest rates.
- ▼ Rising non-interest expenses remain a concern for Prosperity Bancshares. Expenses witnessed a four-year CAGR of 6% (ended 2019). The increase was mainly due to higher salaries and benefits expenses. The same trend expected to continue in the quarters ahead as the company continues to invest in franchises and grow through acquisitions.
- ▼ Weak performance of the mortgage banking business is a big cause of concern for Prosperity Bancshares. Though mortgage income grew in 2019, the majority of it came in the last quarter owing to lower rates and improving consumer sentiments. Nonetheless, the downtrend is likely to continue in the near term as the operating backdrop is not expected to change much.
- ▼ Prosperity Bancshares' trailing 12-month return on equity (ROE) undercuts its growth potential. The company's ROE of 8.04% compares unfavorably with ROE of 10.46% for the industry, underlining the fact that it is less efficient in using shareholder funds compared to its peers.
- ▼ Shares of Prosperity Bancshares have outperformed the industry over the past year. However, the company's 2020 earnings estimates have been revised 6.7% lower over the past 30 days. Therefore, given the concerns and downward estimate revisions, the stock has limited upside potential.

Pressure on margins amid lower interest rates is a major concern for Prosperity Bancshares. Further, mounting operating expenses and weakness in mortgage business are expected to hurt profitability.

Last Earnings Report

Prosperity Bancshares Q4 Earnings Beat, Revenues Up Y/Y - Jan 29, 2020

Prosperity Bancshares fourth-quarter 2019 adjusted earnings of \$1.44 per share surpassed the Zacks Consensus Estimate of \$1.23.

Results were primarily driven by the closure of merger with LegacyTexas Financial Group, Inc. on Nov 1, 2019. The deal supported the company's top-line growth and also resulted in rise in loan and deposit balances. However, increase in operating expenses and a rise in provisions acted as headwinds.

Results in the reported quarter excluded LegacyTexas Financial merger-related charges. Including this, net income available to common shareholders was \$86.1 million or \$1.01 per share compared with \$83.3 million or \$1.19 per share in the prior-year quarter.

Adjusted earnings of \$5.02 per share in 2019 outpaced the consensus estimate of \$4.79. Including merger-related charges, net income available to common shareholders was \$332.6 million or \$4.52 per share compared with \$321.8 million or \$4.61 per share in 2018.

Revenues & Expenses Rise

Net revenues in the quarter were \$267.5 million, up 43.6% from the prior-year quarter. Also, the figure beat the Zacks Consensus Estimate of \$248.7 million.

In 2019, net revenues grew almost 10% to \$820.1 million. Further, it surpassed the Zacks Consensus Estimate of \$801.7 million.

Net interest income was \$232 million, surging 47.6% year over year. The rise was mainly due to merger and higher loan discount accretion. Net interest margin, on a tax-equivalent basis, jumped 50 basis points (bps) to 3.66%.

Non-interest income increased 22.1% to \$35.5 million.

Non-interest expenses jumped 93.6% year over year to \$156.5 million. The increase was largely due to the merger-related expenses, additional expenses related to two months of operations pertaining to the LegacyTexas and lending function.

As of Dec 31, 2019, total loans were \$18.8 billion, up 76.6% from the prior-quarter end. Total deposits grew 42.9% to \$24.2 billion on a sequential basis.

Credit Quality Worsens

Provision for credit losses increased 54.5% to \$1.7 million. Also, net charge-offs were \$1.2 million, rising substantially year over year. As of Dec 31, 2019, total non-performing assets were \$62.9 million, increasing significantly from \$19 million.

However, the ratio of allowance for credit losses to total loans was down 36 bps year over year to 0.46%.

Strong Capital & Profitability Ratios

As of Dec 31, 2019, Tier-1 risk-based capital ratio was 12.30%, compared with 16.32% as of Dec 31, 2018. Moreover, total risk-based capital ratio was 12.70% compared with 16.99% at the end of the year-ago quarter.

Further, common equity tier 1 capital ratio was 12.30%, up from 16.32% in the prior-year quarter.

The annualized return on average assets was 1.19%, down from 1.47%. Annualized return on common equity was 6.33% compared with 8.25% in the prior-year quarter.

Share Repurchase Update

Concurrent with the earnings release, Prosperity Bancshares announced share repurchase authorization of 4.7 million shares. The buyback plan will expire on Jan 28, 2021.

Quarter Ending 12/2019

Report Date	Jan 29, 2020
Sales Surprise	7.58%
EPS Surprise	17.07%
Quarterly EPS	1.44
Annual EPS (TTM)	4.99

Recent News

Prosperity Bancshares Closes Buyout of LegacyTexas Financial – Nov 1, 2019

Prosperity Bancshares has closed the acquisition of LegacyTexas Financial Group, Inc. for \$2.1 billion. The stock and cash transaction, announced in June, has further expanded the company's presence in Texas.

Also, LegacyTexas Bank was merged into Prosperity Bank. LegacyTexas' operations will continue as "Prosperity Bank dba LegacyTexas Bank" till the systems conversion is completed by early June 2020. Following the conversion, the combined entity will operate as Prosperity Bank.

David Zalman, Senior Chairman and Chief Executive Officer of Prosperity Bancshares, said "This transaction represents a milestone in Prosperity's strategic growth and we welcome the LegacyTexas customers and associates to Prosperity Bank. This merger creates one of the largest Texas-based banks by deposits, and makes Prosperity Bank a dominant player in the vibrant markets of Houston and Dallas/Fort Worth."

Deal Details

At the time of announcement, shareholders of LegacyTexas were to receive \$6.28 cash and 0.5280 shares of Prosperity Bancshares for each LegacyTexas share.

Prosperity Bancshares' footprint significantly expanded in and around the Dallas-Fort Worth area as LegacyTexas has 42 branches in 19 cities there. Also, the combined company has \$32 billion of assets, \$24 billion of deposits and a diversified loan portfolio worth \$20 billion.

LegacyTexas President and CEO, Kevin Hanigan, became the President and Chief Operating Officer of Prosperity Bancshares. LegacyTexas EVP and Chief Financial Officer, Mays Davenport will be named as EVP and Director of Corporate Strategy of Prosperity Bancshares.

Further, Prosperity Bancshares increased the size of the company board to 14 and added three LegacyTexas representatives – Kevin Hanigan, Bruce Hunt and George Fisk – to it.

Financial Benefits

At the time of deal announcement, it was noted that it will be accretive to Prosperity Bancshares' earnings by approximately 10.3% in 2020. Also, it will lead to expense savings of 25% of LegacyTexas' non-interest expense base (with 50% phase-in in 2020 and 100% thereafter).

Further, the acquisition is expected enhance Prosperity Bancshares' loan-to-deposit ratio to 71% from 61%. Also, the deal will result in one-time pre-tax charge of \$60 million.

Dividend Update

On Jan 29, Prosperity Bancshares announced a cash dividend of 46 cents per share. The dividend was paid on Apr 1 to shareholders on record as of Mar 16.

Valuation

Prosperity Bancshares' shares are down 29.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 35.5% and 21.4%, over the past year, respectively.

The S&P 500 index is down 1.7% in the past year.

The stock is currently trading at 9.20X forward 12 months earnings, which compares to 10.59X for the Zacks sub-industry, 13.96X for the Zacks sector and 19.53X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.76X and as low as 8.30X, with a 5-year median of 13.98X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$54 price target reflects 9.96X forward earnings.

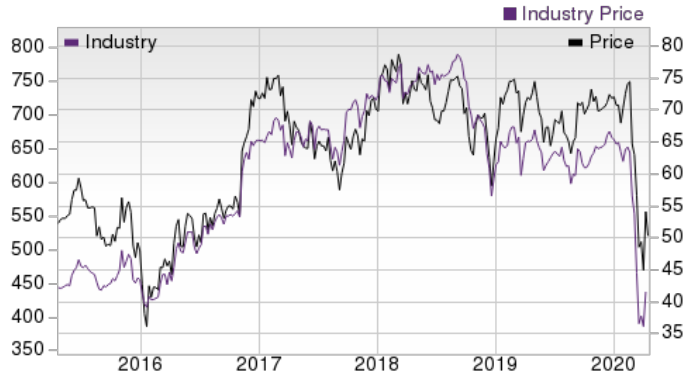
The table below shows summary valuation data for PB

Valuation Multiples - PB					
		Stock	Sub-Industry	Sector	S&P 500
	Current	9.2	10.59	13.96	19.53
5 Yr High		18.76	17.8	16.16	18.53

P/E F12M	5-Year High	18.76	17.8	16.16	19.53
	5-Year Low	8.3	9.78	11.2	15.19
	5-Year Median	13.98	14	13.92	17.45
P/B	Current	0.79	0.89	2.1	3.8
	5-Year High	1.48	2.12	2.9	4.55
	5-Year Low	0.68	0.74	1.71	2.84
	5-Year Median	1.17	1.61	2.52	3.64
P/S F12M	Current	4.18	2.79	4.93	3.2
	5-Year High	8.55	5.22	6.64	3.44
	5-Year Low	3.06	2.74	4.93	2.54
	5-Year Median	5.79	4.2	6.01	3.01

As of 04/20/2020

Industry Analysis Zacks Industry Rank: Bottom 26% (188 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
F.N.B. Corporation (FNB)	Neutral	4
Signature Bank (SBNY)	Neutral	4
Umpqua Holdings Corporation (UMPQ)	Neutral	4
Washington Federal, Inc. (WAFD)	Neutral	3
Commerce Bancshares, Inc. (CBSH)	Underperform	4
Cullen/Frost Bankers, Inc. (CFR)	Underperform	5
Bank OZK (OZK)	Underperform	4
Texas Capital Bancshares, Inc. (TCBI)	Underperform	4

Industry Comparison Industry: Banks - Southwest				Industry Peers		
	PB	X Industry	S&P 500	CBSH	OZK	TCBI
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Underperform	Underperform
Zacks Rank (Short Term)	3	-	-	4	4	4
VGM Score	D	-	-	F	D	C
Market Cap	4.55 B	188.96 M	19.37 B	6.23 B	2.32 B	1.10 B
# of Analysts	9	2	14	8	6	7
Dividend Yield	3.83%	1.63%	2.23%	1.95%	6.01%	0.00%
Value Score	D	-	-	F	A	B
Cash/Price	0.12	0.67	0.05	0.27	0.63	3.65
EV/EBITDA	8.65	5.41	11.66	7.48	2.54	-0.67
PEG Ratio	1.15	1.31	2.20	7.16	0.59	0.80
Price/Book (P/B)	0.76	0.81	2.61	2.09	0.56	0.41
Price/Cash Flow (P/CF)	11.29	7.56	10.30	12.98	5.14	3.13
P/E (F1)	9.80	9.96	17.85	21.48	7.11	6.43
Price/Sales (P/S)	4.75	1.93	2.04	4.30	1.82	0.76
Earnings Yield	10.20%	10.06%	5.48%	4.65%	14.09%	15.54%
Debt/Equity	0.02	0.31	0.71	0.00	0.17	1.04
Cash Flow (\$/share)	4.42	1.99	7.01	4.35	3.57	7.18
Growth Score	D	-	-	D	F	F
Hist. EPS Growth (3-5 yrs)	3.30%	13.60%	10.92%	15.65%	15.48%	22.72%
Proj. EPS Growth (F1/F0)	-2.39%	-11.61%	-3.67%	-27.93%	-23.43%	-45.40%
Curr. Cash Flow Growth	12.62%	12.62%	5.93%	-1.69%	7.01%	8.59%
Hist. Cash Flow Growth (3-5 yrs)	2.48%	14.05%	8.55%	8.41%	28.37%	19.05%
Current Ratio	0.75	0.97	1.24	0.73	1.02	1.21
Debt/Capital	2.06%	23.22%	42.83%	0.08%	14.33%	49.67%
Net Margin	34.66%	22.60%	11.64%	29.06%	33.53%	22.15%
Return on Equity	8.04%	10.62%	16.74%	14.18%	10.57%	12.66%
Sales/Assets	0.04	0.05	0.54	0.06	0.05	0.05
Proj. Sales Growth (F1/F0)	34.71%	0.00%	-0.39%	-3.57%	-6.78%	-8.59%
Momentum Score	C	-	-	F	D	A
Daily Price Chg	-0.64%	-0.08%	-2.18%	-1.54%	0.27%	-6.65%
1 Week Price Chg	-7.04%	-4.94%	0.42%	-3.45%	-7.61%	-17.77%
4 Week Price Chg	15.81%	10.21%	26.24%	22.40%	12.20%	16.49%
12 Week Price Chg	-26.05%	-32.71%	-20.02%	-16.29%	-33.35%	-57.56%
52 Week Price Chg	-29.84%	-32.75%	-12.49%	1.08%	-41.41%	-64.13%
20 Day Average Volume	846,539	27,160	3,036,163	540,764	1,529,684	843,313
(F1) EPS Est 1 week change	0.00%	0.00%	-0.14%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-6.65%	-8.60%	-6.66%	-21.19%	-6.01%	-30.70%
(F1) EPS Est 12 week change	-4.65%	-12.97%	-10.02%	-24.08%	-14.06%	-39.78%
(Q1) EPS Est Mthly Chg	-1.88%	-6.24%	-9.67%	-30.36%	-5.34%	-26.70%

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	D
Momentum Score	C
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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