

Prosperity Bancshares (PB)

\$58.63 (As of 07/29/20)

Price Target (6-12 Months): **\$62.00**

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:B

Value: B

Growth: C

Momentum: B

Summary

Shares of Prosperity Bancshares have outperformed the industry over the past year. The bank's earnings outpaced the Zacks Consensus Estimate in each of the trailing four quarters. Its second-quarter 2020 results reflect loan growth. Solid loan and deposit balances, along with the company's strong balance sheet position are likely to support profitability. Further, opportunistic acquisitions are expected to continue supporting financials. Additionally, the company's steady capital deployment actions seem sustainable and will enhance shareholder value. However, near-zero interest rates and the Federal Reserve's accommodative policy are expected to put pressure on margins. Weakness in the mortgage banking business will likely hurt top-line growth to some extent, which is worrisome. Also, mounting expenses are a matter of concern.

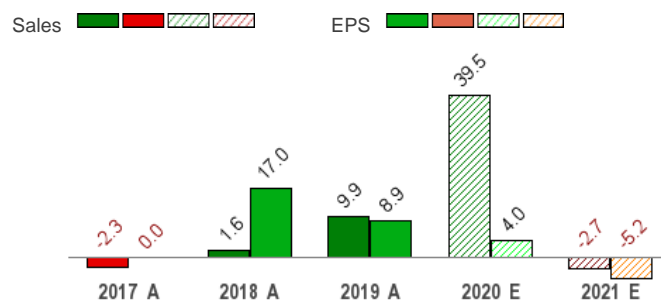
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$75.22 - \$42.02
20 Day Average Volume (sh)	515,475
Market Cap	\$5.4 B
YTD Price Change	-18.5%
Beta	1.47
Dividend / Div Yld	\$1.84 / 3.1%
Industry	Banks - Southwest
Zacks Industry Rank	Bottom 29% (180 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	10.6%
Last Sales Surprise	2.0%
EPS F1 Est- 4 week change	1.4%
Expected Report Date	10/28/2020
Earnings ESP	-1.5%
P/E TTM	11.1
P/E F1	11.2
PEG F1	1.3
P/S TTM	4.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	279 E	281 E	286 E	287 E	1,113 E
2020	290 A	285 A	284 E	286 E	1,144 E
2019	183 A	185 A	185 A	268 A	820 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.28 E	\$1.30 E	\$1.34 E	\$1.36 E	\$4.95 E
2020	\$1.39 A	\$1.25 A	\$1.35 E	\$1.38 E	\$5.22 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.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 07/29/2020. The reports text is as of 07/30/2020.

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*.

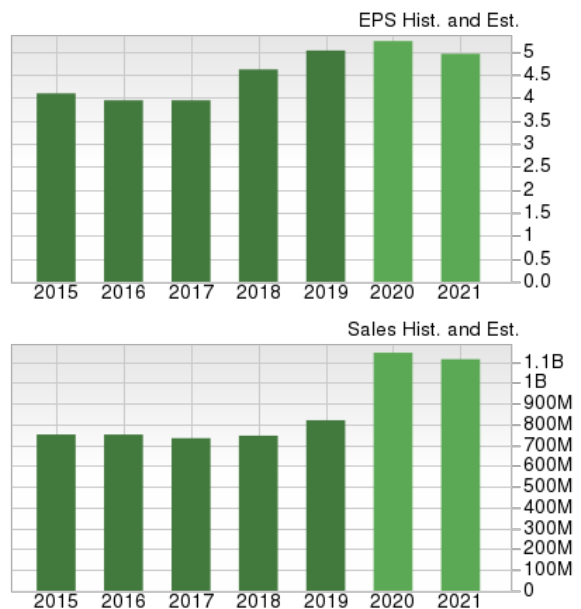
Prosperity Bank provides a wide range of financial products and services — traditional loan and deposit products — to small and medium-sized businesses and consumers. The company provides loans to businesses in the range of \$0.1 million to \$8.0 million. As of Jun 30, 2020, Prosperity Bank operated 275 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, the bank completed the acquisition of LegacyTexas Financial Group, Inc.

As of Jun 30, 2020, Prosperity Bancshares had total assets of \$33 billion, cash and due from banks of \$332.9 million, total loans of \$21 billion, total deposits of \$26.2 billion, as well as shareholders' equity of \$5.9 billion.



Reasons To Buy:

- ▲ 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%, with the trend continuing in first-half 2020. This upside mainly stemmed from higher loan balance and acquisitions. Further, it has been able to improve the deposit mix, with almost 35% being non-interest-bearing deposits as of Jun 30, 2020. A rise in the demand for loans will likely continue to support revenues in the upcoming quarters.
- ▲ 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 acquired LegacyTexas Financial, which will be accretive to earnings in the upcoming quarters. Given a strong balance sheet position, the company is likely to continue with the expansion strategy.
- ▲ As of Jun 30, 2020, Prosperity Bancshares had a total debt of \$593.8 million, and cash and cash equivalents worth \$332.9 million. During second-quarter 2020, the company significantly lowered debt burden. Its other borrowings were down 92.2% sequentially. Further, its times interest earned — which was 25.8X at second quarter-end — has been improving over the last several quarters. This implies that the company's earnings are likely to be sufficient to meet interest and/or debt obligations if the economic situation worsens.
- ▲ 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 solid earnings strength, capital deployment activities are projected to remain sustainable.
- ▲ Shares of Prosperity Bancshares have outperformed the industry over the past year. Moreover, the company's 2020 earnings estimates have been revised 1.4% upward over the past 30 days. Further, the stock seems undervalued than the broader industry. Its current price/earnings (F1) and PEG ratios are below the respective industry averages. It has a Value Score of B. Therefore, given the strong fundamentals and positive estimate revisions, the stock has decent upside potential.

Inorganic expansion efforts, higher loan balance and a 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 pressure owing to 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 uptrend persisted in the first six months of 2020. 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. For second-quarter 2020, the same declined on a sequential basis despite historically low mortgage rates. Dismal mortgage performance is likely to continue in the near term, as the operating backdrop is not expected to change much.

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

Last Earnings Report

Prosperity Bancshares Q2 Earnings Beat, Revenues Down Y/Y

Prosperity Bancshares Inc.'s second-quarter 2020 adjusted earnings per share of \$1.25 surpassed the Zacks Consensus Estimate of \$1.09. However, the bottom line decreased 10.1% from the first quarter.

The results were primarily driven by an increase in net interest income. The company's balance sheet position remained strong during the quarter. However, higher expenses, decline in fee income and a drastic jump in provision for credit losses were the undermining factors.

After considering merger-related charges and income tax benefit, net income available to common shareholders was \$130.9 million, which was relatively stable on a sequential basis.

Revenues Down, Expenses Rise

Net revenues were \$284.6 million, down 2% from the prior quarter. Nonetheless, the figure beat the Zacks Consensus Estimate of \$279 million.

Net interest income was \$259 million, up 1.1% from the first quarter. The increase was primarily driven by lower interest expense, partially offset by a decrease in loan discount accretion and interest income on securities.

Net interest margin, on a tax-equivalent basis, declined 12 basis points (bps) sequentially to 3.69%.

Non-interest income plunged 25.3% year over year to \$25.7 million. The fall was mainly due to a loss on write-down of assets and decrease in NSF fees.

Non-interest expenses increased 7.7% from the first quarter to \$134.4 million. The increase was largely due to merger-related expenses, and salaries and benefits costs.

As of Jun 30, 2020, total loans were \$21 billion, up 9.9% from first quarter-end. Total deposits rose 9.8% sequentially to \$26.2 billion.

Credit Quality Worsens

Provision for credit losses was \$10 million compared with no provisions in first-quarter 2020. Net charge-offs were \$13 million, up substantially from \$0.8 million in the first quarter.

As of Jun 30, 2020, total non-performing assets were \$77.9 million, which increased 15.9% sequentially. However, the ratio of allowance for credit losses to total loans was 1.54%, down 17 bps from the first quarter.

Capital Ratios Improve, Profitability Ratios Worsen

As of Jun 30, 2020, Tier-1 risk-based capital ratio was 12.29%, up from 12.27% on Mar 31, 2020. Moreover, total risk-based capital ratio was 13.36% compared with 12.27% at first quarter-end.

The annualized return on average assets was 1.61%, down from 1.67% at first quarter-end. Annualized return on common equity was 8.84% compared with 8.86% in the first quarter.

Share Repurchase Update

During the quarter, the company did not repurchase any shares.

Outlook

For the third quarter 2020, core NIM is expected to be relatively stable, given the current economic conditions, with some additional pressure owing to loan repricing.

Non-interest expenses are anticipated within \$118-\$119 million. This excludes additional cost savings of nearly \$7-\$9 million per quarter from the LegacyTexas Financial acquisition.

Quarter Ending 06/2020

Report Date	Jul 29, 2020
Sales Surprise	2.00%
EPS Surprise	10.62%
Quarterly EPS	1.25
Annual EPS (TTM)	5.27

Recent News

Dividend Update

On Jul 29, Prosperity Bancshares announced a cash dividend of 46 cents per share. The dividend will be paid on Oct 1 to shareholders of record as of Sep 15.

Valuation

Prosperity Bancshares' shares are down 18.4% in the year-to-date period and 15.5% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 24.5% and 17.1% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector are down 20.9% and 11.8%, respectively.

The S&P 500 index is up 0.1% in the year-to-date period and 8.5% in the past year.

The stock is currently trading at 11.58X forward 12 months earnings, which compares to 14.52X for the Zacks sub-industry, 16.31X for the Zacks sector and 22.44X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.76X and as low as 8.19X, with a 5-year median of 13.93X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$62 price target reflects 12.25X forward earnings.

The table below shows summary valuation data for PB

Valuation Multiples - PB					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	11.58	14.52	16.31	22.44
	5-Year High	18.76	17.87	16.31	22.44
	5-Year Low	8.19	10.53	11.59	15.25
	5-Year Median	13.93	14.18	14.16	17.52
P/TB TTM	Current	2.18	1.55	3.33	12.7
	5-Year High	3.18	2.92	4	12.94
	5-Year Low	1.39	1.06	2.01	5.96
	5-Year Median	2.37	2.17	3.48	9.53
P/S F12M	Current	4.82	3.37	6.04	3.54
	5-Year High	8.55	5.29	6.66	3.54
	5-Year Low	3.06	2.74	4.96	2.53
	5-Year Median	5.77	4.16	6.06	3.02

As of 07/10/2020

Industry Analysis Zacks Industry Rank: Bottom 29% (180 out of 253)



Top Peers

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

Industry Comparison Industry: Banks - Southwest				Industry Peers		
	PB	X Industry	S&P 500	CBSH	OZK	TCBI
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	B	-	-	F	D	B
Market Cap	5.43 B	188.43 M	22.69 B	6.48 B	3.20 B	1.70 B
# of Analysts	9	2.5	14	9	7	7
Dividend Yield	3.14%	1.37%	1.8%	1.86%	4.41%	0.00%
Value Score	B	-	-	C	B	B
Cash/Price	0.07	0.76	0.07	0.41	0.52	6.15
EV/EBITDA	10.47	4.98	13.11	6.27	4.52	-9.18
PEG Ratio	1.28	5.02	3.05	NA	NA	18.41
Price/Book (P/B)	0.91	0.85	3.15	2.02	0.78	0.66
Price/Cash Flow (P/CF)	13.27	9.60	12.28	13.36	6.91	4.69
P/E (F1)	10.87	14.23	22.27	25.49	15.88	147.26
Price/Sales (P/S)	4.65	2.02	2.46	4.60	2.63	1.24
Earnings Yield	8.90%	7.04%	4.25%	3.92%	6.31%	0.68%
Debt/Equity	0.02	0.25	0.75	0.00	0.30	1.20
Cash Flow (\$/share)	4.42	1.71	6.94	4.35	3.57	7.18
Growth Score	C	-	-	F	F	C
Hist. EPS Growth (3-5 yrs)	4.67%	15.63%	10.85%	13.21%	7.35%	17.59%
Proj. EPS Growth (F1/F0)	4.07%	-22.23%	-7.70%	-36.31%	-52.86%	-96.33%
Curr. Cash Flow Growth	12.62%	8.59%	5.31%	-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	0.79	1.00	1.31	0.72	0.99	1.19
Debt/Capital	2.06%	19.78%	44.23%	0.04%	23.27%	53.10%
Net Margin	36.72%	20.84%	10.45%	21.82%	21.95%	8.10%
Return on Equity	8.25%	7.96%	14.99%	10.03%	6.49%	6.68%
Sales/Assets	0.04	0.05	0.53	0.05	0.05	0.04
Proj. Sales Growth (F1/F0)	39.54%	0.00%	-1.97%	-2.92%	-2.23%	-4.52%
Momentum Score	B	-	-	D	F	C
Daily Price Chg	5.62%	0.44%	1.52%	2.50%	2.96%	6.25%
1 Week Price Chg	2.31%	2.17%	0.37%	3.37%	3.89%	15.28%
4 Week Price Chg	1.44%	-1.51%	5.44%	0.40%	9.48%	13.87%
12 Week Price Chg	2.14%	2.14%	15.38%	1.47%	21.01%	34.64%
52 Week Price Chg	-15.51%	-29.56%	-1.61%	0.32%	-19.20%	-46.51%
20 Day Average Volume	515,475	17,372	1,846,377	493,084	977,582	536,315
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.20%	0.55%	-0.59%
(F1) EPS Est 4 week change	1.45%	4.70%	0.27%	-3.39%	-0.37%	24.13%
(F1) EPS Est 12 week change	2.87%	-2.13%	-0.85%	-6.26%	-15.52%	-0.12%
(Q1) EPS Est Mthly Chg	1.25%	0.00%	0.13%	7.62%	-2.08%	34.29%

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	C
Momentum Score	B
VGM Score	B

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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