

Texas Capital (TCBI)

\$27.65 (As of 05/01/20)

Price Target (6-12 Months): **\$24.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 03/30/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:F

Value: C

Growth: F

Momentum: F

Summary

Shares of Texas Capital have underperformed the industry, over the past six months. Also, the company has a dismal earnings surprise history, having beaten the Zacks Consensus Estimate in only one of the trailing four quarters. The first-quarter 2020 net loss underscored elevated expenses, pressure on margin, fall in revenues and high provisions. Texas Capital's persistently rising costs will likely impede its bottom-line growth. Also, high exposure to commercial and real estate loans and debt level are headwinds. Yet, rising loans and deposits balance suggests a strong capital position, which will help the company undertake expansions. Texas Capital's recent all-stock merger of equals with Independent Bank Group reflects the companies' efforts for business expansion. Nevertheless, deterioration in credit quality is a concern.

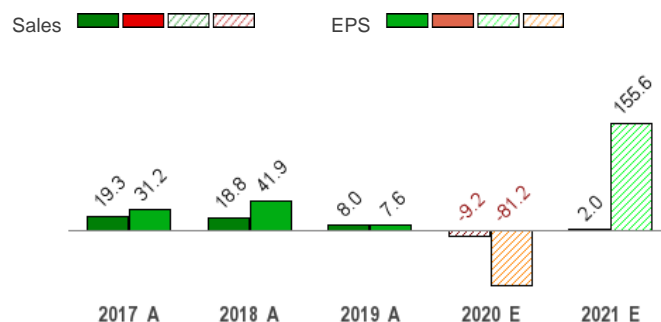
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$66.61 - \$19.10
20 Day Average Volume (sh)	971,433
Market Cap	\$1.4 B
YTD Price Change	-51.3%
Beta	2.18
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Banks - Southwest
Zacks Industry Rank	Bottom 13% (219 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-111.7%
Last Sales Surprise	-4.0%
EPS F1 Est- 4 week change	-59.1%
Expected Report Date	NA
Earnings ESP	-23.3%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	233 E	241 E	247 E	245 E	992 E
2020	240 A	243 E	245 E	241 E	973 E
2019	266 A	268 A	272 A	266 A	1,072 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.46 E	\$0.61 E	\$0.79 E	\$0.80 E	\$2.99 E
2020	-\$0.11 A	\$0.49 E	\$0.70 E	\$0.67 E	\$1.17 E
2019	\$1.60 A	\$1.50 A	\$1.70 A	\$1.44 A	\$6.23 A

*Quarterly figures may not add up to annual.

P/E TTM	6.1
P/E F1	23.6
PEG F1	2.3
P/S TTM	1.0

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 05/01/2020. The reports text is as of 05/04/2020.

Overview

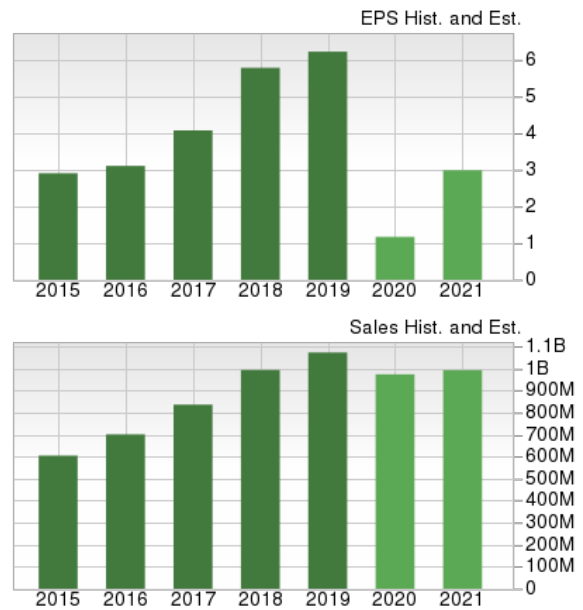
Texas Capital Bancshares Inc., a financial holding company, is the parent company of Texas Capital Bank, a Texas-based bank headquartered in Dallas. The company focuses on leveraging local business and community ties to the five major metropolitan areas of Texas — Dallas, Houston, Fort Worth, Austin and San Antonio. All of its business activities are conducted through its bank subsidiary. The company was founded in November 1996, and commenced operations in December 1998.

While the Texas market continues to be central to the company's growth and success, it has developed several lines of business, including mortgage finance, mortgage correspondent aggregation ("MCA"), homebuilder finance, insurance premium finance, lender finance and asset-based lending, that offer specialized loan and deposit products to businesses regionally and across the nation.

Texas Capital focuses primarily on middle-market business customers and high-net-worth individuals in each of the five major metropolitan markets of Texas. For its business customers, the company offers commercial loans for general corporate purposes including financing for working capital, internal growth, acquisitions and financing for business insurance premiums. Additionally, the company provides real estate term and construction loans, equipment leasing, cash management services, trust and escrow services and letters of credit.

The company also provides complete banking services for its individual customers, including personal trust and wealth management services, certificates of deposit, interest bearing and non-interest bearing checking accounts with optional features such as Visa debit/ATM cards and overdraft protection, traditional money market and savings accounts, consumer loans (both secured and unsecured), branded Visa credit card accounts including gold-status accounts and internet banking.

As of Mar 31, 2020, Texas Capital had total assets of around \$35.9 billion, loans of \$25.2 billion and deposits of \$27.1 billion.



Reasons To Sell:

- ▼ The company continues to see a rise in expenses, witnessing a CAGR of 15.9% over the last five years (2015-2019), with the increasing trend continuing in first-quarter 2020. Though the company's efforts to hire experienced bankers and expand its presence are encouraging, the resultant expenses, which continue to rise at the rate higher than the revenues, negate the incremental effects of business expansion.
- ▼ Deterioration in credit quality metrics remain a headwind for Texas Capital. The company witnessed an increase in non-performing assets and higher charge-offs primarily related to energy loans during 2016, and while those levels have moderated in 2017 and 2018, they still remain elevated compared to the overall loan portfolio. Furthermore, the metrics have increased in 2019 with some quarterly volatility. Therefore, continuation of such trend can be risky for the company amid challenging global economy and competitive markets.
- ▼ Amid the coronavirus crisis and its related impact on economy, the company holds a debt level of \$5.6 billion and debt-capital ratio of 65.4 (above the industry's average of 23.22), which has witnessed volatility in the past few quarters and a substantial increase in first-quarter 2020. Therefore, with a declining time-interest-earned ratio of 5 over the past few quarters, which indicates the company's ability to meet its debt obligations based on current income, we believe Texas Capital carries a higher credit risk, and an enhanced likelihood of default of interest and debt repayments if the economic situation worsens.
- ▼ Texas Capital's business is concentrated geographically in Texas, with management's focus being limited on diversification as compared to some of its peers. We anticipate that lack of diversifying efforts will potentially hamper its top- and bottom-line growth in the future.
- ▼ Shares of Texas Capital have underperformed the industry over the past six months. With this unfavorable trend, the company's current-year earnings estimates have been revised 63.8% downward, over the past 30 days. Also, the stock seems overvalued when compared with the broader industry. Its current price-to-earnings (P/E) (F1) and PEG ratios are above the respective industry averages. Therefore, given the above concerns and lack of positive estimate revisions, we find the stock has limited upside potential.

Deterioration in credit quality and lack of geographical diversification remain concerns for Texas Capital. Additionally, escalating expenses on hiring of experienced bankers is a near term headwind.

Risks

- Organic growth is a key strength at Texas Capital, as reflected by its revenue-growth story. Though revenues declined in first-quarter 2020 on low rates and decline in fee income, the figure witnessed a compounded annual growth rate (CAGR) of 15.4% over the last five years (2015-2019), primarily due to elevated net interest income, driven by rise in average earning assets, as well as rise in non-interest income. Further, a diversified fee income base and rising average earning assets will keep supporting revenue growth in the near term.
 - With the gradual change in the rate environment, margin pressure for Texas Capital eased. After facing a declining trend for years, the company reported a stabilized net interest margin (NIM) in 2016 and improvement in 2017 and 2018, as a result of rate hikes since December 2016. Also, the company has been benefiting from better fee pricing and improved loan yields. Amid the Fed's accommodative monetary-policy stance, though 2019 and first-quarter 2020 witnessed contraction of margin on account of rise in deposit costs and low rates, improvement in economy and decent loan growth might support margins.
 - Growth remains the key story at Texas Capital, and it continues to perform well on a variety of metrics. The company continued to experience growth in total loans held for investment (CAGR of around 10.2%) and deposits (CAGR of 15.1%) over the last five years (2015-2019). The increasing trend continued in first-quarter 2020 as well. We believe this growth has stemmed from a gain in market share from the company's economizing competitors which struggled against Texas Capital's relationship-based model.
 - The company's capital ratios remain above the levels required to be considered well capitalized and have been enhanced with the additional capital raised since 2008. As of Mar 31, 2020, the ratio of tangible common equity to total tangible assets was 7.3%. We believe its strong capital position would help it undertake opportunistic expansions in the foreseeable future.
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Last Earnings Report

Texas Capital Reports Q1 Loss, Costs Rise

Texas Capital reported adjusted loss per share of 11 cents in first-quarter 2020, against the Zacks Consensus Estimate for earnings of 94 cents. The reported figure excluded certain noteworthy items such as the impacts of the MSR impairment charges and merger-related expenses.

Elevated expenses and pressure on margin were negatives. Further, results reflect a decline in loan balances. Also, a fall in revenues, a substantial rise in provisions and reserve build related to the coronavirus-led crisis were other key headwinds.

After considering one-time items, net loss available to common stockholders was \$19.1 million or 38 cents per share against net income of \$80.4 million or \$1.60 per share recorded in the prior-year quarter.

Revenues Rise, Costs Escalate

Total revenues declined 9.4% year over year to \$240.1 million in the first quarter due to lower net interest and non-interest income. Furthermore, revenues lagged the Zacks Consensus Estimate of \$244.6 million.

Texas Capital's net interest income was \$228.3 million, down 3.1% year over year, mainly stemming from a decline in loan yields, partly muted by a decrease in funding costs. Net interest margin, however, contracted 95 basis points (bps) year over year to 2.78%.

Non-interest income declined 61% year over year to \$17.8 million. The downside primarily resulted from lower other non-interest income, partially offset by increases in brokered loan fees, servicing income and swap fees.

Non-interest expenses flared up 17.8% year over year to \$165.4 million. The upswing mainly resulted from a rise in almost all components of expenses, partly negated by lower marketing expenses.

As of Mar 31, 2020, total loans declined 7.7% on a sequential basis to \$25.2 billion, while deposits rose 2.3% sequentially to \$27.1 billion.

Credit Quality Deteriorates

Non-performing assets totaled 0.9% of the loan portfolio plus other real estate-owned assets compared with the prior-year quarter's figure of 0.57%. Total non-performing assets rose 64% to \$219.2 million compared with the prior-year quarter.

Provisions for credit losses summed \$96 million compared with \$20 million in the year-ago quarter. The company's net charge-offs were \$57.7 million compared with \$4.6 million as of Mar 31, 2019.

Capital Ratios Steady

The company's capital ratios displayed a steady position during the first quarter. Tangible common equity to total tangible assets came in at 7.3% compared with the year-earlier quarter's 8.5%.

Common equity Tier 1 ratio was 9.3%, up from 8.6% in the prior-year quarter. Leverage ratio was 8.5% compared with 10% as of Mar 31, 2019.

Stockholders' equity was up 8.6% year over year to \$2.8 billion as of Dec 31, 2019. The uptrend chiefly allied with the retention of net income.

Quarter Ending **03/2020**

Report Date	Apr 22, 2020
Sales Surprise	-4.01%
EPS Surprise	-111.70%
Quarterly EPS	-0.11
Annual EPS (TTM)	4.53

Recent News

Texas Capital & Independent Bank to Merge in Deal Worth \$5.5 Billion - Dec 9, 2019

Texas Capital entered into a stock-cash acquisition deal with Independent Bank Group, Inc, per which the former will merge with the latter in an all-stock merger of equals. The combined holding entity will operate under the name of Independent Bank Group, headquartered at McKinney, TX, while the name of the combined bank will be Texas Capital.

Additionally, retaining the Independent Financial branding, operations in retail locations in Colorado will continue. The combined company, for a total market value of \$5.5 billion, will trade under the symbol "IBTX" on the Nasdaq Stock Market.

The deal, approved by the boards of both banks, on completion will be listed as a premier Texas-based super regional bank.

The combined entity is aimed at capturing market opportunities and boosting client base. Moreover, the companies' expanded scale, technological advancement and increased product offerings will help capitalize its market share.

However, the deal awaits certain customary approvals by shareholders of both companies and other closing conditions. The transaction is anticipated to close in mid-2020.

Terms of the Deal

Per the terms of the deal, each common shareholder of Texas Capital will get stock equivalent to 1.0311 of Independent Bank Group shares for every Texas Capital share held. Specifically, Texas Capital shareholders in total will own about 55% of the combined entity, while shareholders of Independent Bank Group will own the remaining.

Further, shareholders of the combined entity will be entitled to an annualized dividend on common stock of \$1.00 per share after the deal's closure, subject to board of directors' approval.

Texas Capital and Independent Bank Group will create the combined entity, with \$48 billion in assets. Strategically, the combined entity will enhance through advanced technologies, innovative products and core deposit business, creating a competitive edge in Texas.

Also, the combination will cater various needs of businesses, professionals and individuals with diversified products. On completion, Texas Capital and Independent Bank Group, maintaining the strong working cultures, aim to offer superior client services.

Members from both Texas Capital and Independent Bank Group will lead the combined entity. The organization's board of directors will include seven directors from Texas Capital and six from Independent Bank Group. Independent Bank Group chairman and CEO David R. Brooks will lead as chairman, president and CEO of the combined entity, while Texas Capital president and CEO C. Keith Cargill will act as a special advisor to the CEO assisting in retaining clients and serve as advisor on key strategic initiatives.

Financial Benefits

Cost synergies are anticipated to approximate around \$170 million on annual run-rate cost savings, boosting profitability and supporting sustained growth.

Per Texas Capital's expectations, the deal is likely to be 14% accretive to earnings by the first full year post closure, while around 27% TBVPS accretion and 26% EPS accretion is expected for Independent Bank Group. Such expectations assume 75% phase-in of cost savings.

The combined entity is likely to record operating and return metrics with cost savings on 75% phased-in basis, on a pro forma basis. Notably, return on tangible common equity is likely to approximate 15%, while return on average assets is projected at 1.3%.

Valuation

Texas Capital's shares are down 51.3% in the year-to-date period and 58.3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 31.1% and 26.4%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry and the sector are down 30.3% and 22%, respectively.

The S&P 500 Index is down 12.1% in the year-to-date period and down 3.7% in the past year.

The stock is currently trading at 13.48X forward 12 months earnings, which compares to 13.73X for the Zacks sub-industry, 14.86X for the Zacks sector and 20.18X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.43X and as low as 3.92X, with a 5-year median of 14.69X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$24 price target reflects 11.71X forward earnings.

The table below shows summary valuation data for TCBI

Valuation Multiples - TCBI					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.48	13.73	14.86	20.18
	5-Year High	26.43	17.8	16.18	20.18

P/TB TTM	5-Year Low	3.92	9.78	11.24	15.19
	5-Year Median	14.69	14.06	13.94	17.44
	Current	0.54	1.49	2.43	10.69
	5-Year High	2.58	2.84	4	12.78
	5-Year Low	0.37	1.05	1.99	6.02
P/S F12M	5-Year Median	1.74	2.2	3.47	9.19
	Current	1.42	3.18	4.98	3.19
	5-Year High	5.71	5.22	6.7	3.44
	5-Year Low	0.98	2.73	4.98	2.54
	5-Year Median	3.57	4.21	6.06	3.01

As of 05/01/2020

Industry Analysis Zacks Industry Rank: Bottom 13% (219 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
New York Community Bancorp, Inc. (NYCB)	Neutral	2
Bank OZK (OZK)	Neutral	4
Prosperity Bancshares, Inc. (PB)	Neutral	3
Associated Banc-Corp (ASB)	Underperform	5
BankUnited, Inc. (BKU)	Underperform	3
BancorpSouth Bank (BXS)	Underperform	5
Hancock Whitney Corporation (HWC)	Underperform	5
Zions Bancorporation, N.A. (ZION)	Underperform	5

Industry Comparison Industry: Banks - Southwest				Industry Peers		
	TCBI	X Industry	S&P 500	HWC	OZK	PB
Zacks Recommendation (Long Term)	Underperform	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	5	-	-	5	4	3
VGM Score	F	-	-	D	F	F
Market Cap	1.39 B	223.54 M	20.61 B	1.72 B	2.75 B	5.55 B
# of Analysts	4	3	14	9	7	10
Dividend Yield	0.00%	1.52%	2.11%	5.46%	5.07%	3.14%
Value Score	C	-	-	A	B	D
Cash/Price	7.36	0.68	0.06	0.33	0.59	0.12
EV/EBITDA	-5.41	6.17	11.87	3.16	3.42	10.58
PEG Ratio	2.29	1.95	2.47	1.31	0.96	1.20
Price/Book (P/B)	0.53	0.91	2.67	0.50	0.66	0.93
Price/Cash Flow (P/CF)	3.87	8.59	10.66	4.18	6.33	13.57
P/E (F1)	23.63	12.91	19.01	10.45	11.58	11.96
Price/Sales (P/S)	0.98	2.10	2.10	1.18	2.20	5.17
Earnings Yield	4.23%	7.71%	5.05%	9.56%	8.63%	8.35%
Debt/Equity	2.00	0.31	0.72	0.10	0.17	0.02
Cash Flow (\$/share)	7.18	1.99	7.01	5.01	3.57	4.42
Growth Score	F	-	-	F	F	D
Hist. EPS Growth (3-5 yrs)	21.32%	13.60%	10.88%	24.55%	11.77%	3.30%
Proj. EPS Growth (F1/F0)	-81.18%	-23.96%	-7.32%	-52.84%	-44.20%	-2.53%
Curr. Cash Flow Growth	8.59%	12.62%	5.92%	1.88%	7.01%	12.62%
Hist. Cash Flow Growth (3-5 yrs)	19.05%	14.05%	8.55%	9.27%	28.37%	2.48%
Current Ratio	1.29	0.97	1.23	0.82	1.02	0.75
Debt/Capital	65.39%	23.22%	43.84%	9.43%	14.33%	2.06%
Net Margin	15.73%	21.99%	11.08%	9.42%	26.16%	35.42%
Return on Equity	9.11%	9.61%	16.44%	4.70%	8.02%	8.80%
Sales/Assets	0.04	0.05	0.54	0.05	0.05	0.04
Proj. Sales Growth (F1/F0)	-9.24%	0.00%	-1.42%	0.68%	-5.36%	34.73%
Momentum Score	F	-	-	C	F	D
Daily Price Chg	-4.11%	-3.02%	-2.39%	-3.19%	-1.31%	-1.90%
1 Week Price Chg	8.27%	0.14%	-1.74%	2.39%	7.85%	1.69%
4 Week Price Chg	25.59%	11.10%	17.07%	15.02%	37.93%	27.48%
12 Week Price Chg	-51.54%	-28.96%	-18.53%	-49.04%	-19.19%	-17.76%
52 Week Price Chg	-57.46%	-28.76%	-9.82%	-52.20%	-32.03%	-18.46%
20 Day Average Volume	971,433	23,957	2,641,413	813,850	1,889,358	833,922
(F1) EPS Est 1 week change	-24.62%	0.00%	0.00%	0.00%	-19.29%	-0.30%
(F1) EPS Est 4 week change	-59.06%	-1.73%	-6.62%	-30.41%	-24.93%	-2.06%
(F1) EPS Est 12 week change	-71.82%	-24.06%	-13.28%	-46.31%	-37.37%	-12.68%
(Q1) EPS Est Mthly Chg	-44.89%	-1.28%	-11.97%	-51.36%	-33.61%	-4.42%

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	C
Growth Score	F
Momentum Score	F
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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