

## 10 Banks With Earnings Upside Potential

Lauren Tara LaCapra

11/17/10 - 07:00 AM EST

NEW YORK (TheStreet) - Reserve releasing has been padding the bottom line of big banks for a few quarters now, leaving room for speculation regarding how the practice could impact earnings in the future.

The initial wave of reserve releasing came as a surprise, helping spur a bank-stock rally through mid-April. Then, as "double-dip" recession became all but a foregone conclusion, Wall Street began questioning whether big banks' reserve releasing had come too much, too soon. Bank stocks approached 52-week lows by late-summer.

Just as the market started to regain confidence in CEOs' assertions that major lenders were well-capitalized and adequately reserved, a wave of mortgage scandals erupted - raising fresh questions about their reserves against repurchases and litigation.

But, in the past couple of weeks, concerns over the robo-signing scandal and buyback losses seemed to have died down from a firestorm to a campfire. A Congressional Oversight Panel report on Tuesday pegged potential buyback losses for the entire financial industry at \$52 billion - a healthy portion of which has already been booked or reserved against and a far cry from the \$375 billion cited for Bank of America alone earlier this month.

As a result, Wall Street seems newly convinced that the reserve-releasing trend will continue. Bulls suggest that analyst estimates may not fully reflect the upside from credit-book improvements over the next year or two.

**"Not all of it has been baked in," says Yu-Dee Chang, chief principal of ACE Investment Strategists. "About half of it has been baked in."**

**In particular, Chang sees upside in Bank of New York Mellon (BK), which has reserves but much less exposure to loan-losses as a so-called "banker's bank," which mainly provides services to other lenders. He also thinks PNC Financial Services(PNC), U.S. Bancorp (USB) and JPMorgan Chase (JPM) could see some extra earnings cushion from reserve releasing because of the quality of their loan portfolios.**

The question is whether the market realizes this upside potential yet - and whether it matters. Reserve releasing has been shrugged off by bearish investors who are looking for core revenue growth before plunging into bank stocks. Even Chang characterizes the reserve-release boost as hollow profit. But what he's hearing on Wall Street is that double-dip fears are over and bank stocks are once again a buy.

**"It is going to be beneficial to their earnings, artificially of course," says Chang, whose firm manages \$155 million. "So it's kind of a speculative play, for somebody who is a little more daring. But I do believe these banks will start drawing down on the reserves, boosting earnings. I believe these banks are a buy."**

*TheStreet* performed an analysis of data supplied by SNL Financial to determine which banks have lagged competitors in reserve-releasing. While reserves are released according to formulas prescribed by accounting standards boards, there are a handful of banks that appear to be "over-reserved" - meaning they may surprise investors with bombastic earnings because of how much cash they're able to move from the reserve silo into the bottom line.

We ranked banks by asset size, then examined the overall level of loan-loss reserve coverage to the annualized net charge-off ratio for the first three quarters of 2010.

The following 10 holding companies appear to be over-reserved by the widest margin, in a range of 1.3 to 3.0 percentage points. They represent a diverse group of lenders - some of which appear solidly capitalized with improving credit quality, others that are still in the eye of the credit storm and

still others that still owe bailout funds to the government:



## 10. Fulton Financial Corporation

Company Profile

Shares of **Fulton Financial** (FULT) of Lancaster, Penn. closed at \$9.06

Friday, rising 14% over the previous year. The company operates seven affiliate banks, down from 15 a year ago, and in October merged **Delaware National Bank** into its largest subsidiary, **Fulton Bank**.

Fulton's loan loss reserves covered 2.34% of total loans as of September 30 and the company's ratio of net loan charge-offs to average loans for the first three quarters was 1.03% -- the lowest among the 10 banks listed here. The company fully repaid \$376.5 million in TARP money in July, after raising \$230 million in common equity through a public offering in June.

### Income Statement

Third-quarter net income available to common shareholders was \$31.5 million, or 16 cents a share, rising from \$26.6 million, or 14 cents a share, the previous quarter and \$18.3 million, or 10 cents a share, a year earlier.

During the third quarter, Fulton's provision for loan losses was \$40 million, which was the same level for the second quarter and down only slightly from \$45 million a year earlier. Since net charge-offs - loan losses less recoveries - totaled \$38.8 million, the company was still building reserves.

Fulton reported a net interest margin - essentially the difference between the average yield on loans and securities and the average cost of funds - of 3.81% for the third quarter, improving from 3.76% in the second quarter and 3.55% for the third quarter of 2009. The industry trend has been for margin improvement despite weak loan demand, as banks have taken advantage of declining funding costs in a low interest rate environment. Fulton's margin was also boosted because non-interest

bearing demand deposits increased 11% year-over-year to \$2.1 billion as of September 30, while total liabilities declined 2% to \$14.4 billion.

David Darst of Guggenheim Securities expects the margin to benefit during the fourth quarter as \$80 million in Federal Home Loan Bank borrowings mature, which Fulton can repay "with excess liquidity which would reduce the balance sheet without a negative impact on earnings."

## Balance Sheet

Fulton had total assets of \$16.3 billion as of September 30. Nonperforming assets - including nonaccrual loans, loans past due 90 days or more, and repossessed real estate - comprised 2.18% of total assets, increasing from 2.06% the previous quarter and 1.82% a year earlier, with the rise in problem assets during the third quarter occurring "primarily in construction loans, commercial loans and residential mortgages," according to the company.

CEO Scott Smith said during the company's third-quarter earnings conference call that "economic problems and related credit issues persist," and chief operating officer Phil Wenger said two large residential construction loans were moved to nonaccrual status even though the loans were technically current, because "the pace of repayment or sales was not occurring and acceptable level."

David Darst maintained his buy rating for Fulton with an \$11 price target following the third-quarter earnings release, however, he lowered his 2011 earnings estimate to 80 cents a share from 86 cents a share, in part because "credit trends have yet to improve."

Fulton Financial had a Tier 1 leverage ratio of 9.22% and a total risk-based capital ratio of 13.94% as of September 30, well above the 5% and 10% required for most banks and thrifts to be considered well-capitalized by regulators. The second ratio reflects asset quality and reserve coverage, and is the one that most commonly falls below regulatory thresholds. Fulton's capital position is strong, especially since the company is profitable. The company's tangible common equity ratio was 8.41% as of September 30 - the highest among the banks listed here.

## Stock Ratios

The shares trade for 1.4 times tangible book value, according to SNL Financial, and 11.9 times the consensus earnings estimate of 76 cents a share for 2011, among analysts polled by Thomson Reuters. The forward price-to-earnings ratio drops to 9.6, based on the 2012 consensus earnings estimate of 94 cents a share.



## Analyst Ratings

Out of 12 analysts covering Fulton Financial, four rate the shares a buy and the other eight analysts recommend investors hold the shares.

## 9. First BanCorp

### Company Profile

Shares of **First BanCorp**(FBP) of San Juan, Puerto Rico closed at 30 cents on Friday, dropping 82% over the previous year, as the company has booked very large losses as it boosted loan loss reserves.

First BanCorp's loan loss reserves covered 4.99% of total loans as of September 30, while its net charge-off ratio for the first three quarters of 2010 was 3.67%.

### Income Statement

For the third quarter, First Bancorp reported net income to common shareholders of \$363.4 million, or 28 cents per diluted share, compared to a second-quarter net loss to common shareholders of \$96.8 million, or \$1.05 a share, and a loss of \$174.7 million, or \$1.89 a share a year earlier.

The third-quarter profit reflected \$440.5 million in gains from the August conversion of \$487 million in preferred shares to common shares at heavy discounts.

In July, First Bancorp exchanged the \$400 million in preferred shares held by the U.S. Treasury Department for bailout money received via TARP for \$424.2 million in mandatorily convertible preferred shares.

First BanCorp is also in the midst of another \$500 million common stock offering, which has yet to be priced. The conversion of the Treasury's new convertible shares to common shares is set to take place after this offering is completed.

The capital moves are part of the company's plan to meet regulators requirements to increase its Tier 1 leverage ratio to 8% and its total risk-based capital ratio to 12%. These ratios were 8.34% and 13.26% as of September 30, according to SNL Financial.

Excluding the gains from share exchanges, First BanCorp's net loss for the third quarter was \$75.2 million. The provision for loan and lease losses was \$120.5 million, declining from \$146.8 million in the second quarter and \$148.1 million during the third quarter of 2009. Net charge-offs totaled \$116.3 million, so the bank was still building reserves.

Pre-provision, pre-tax income for the third quarter was \$43.4 million, rising 22% from the previous quarter, although it was down 30% from a year earlier. In a report titled "FBP Shareholders Waiting to Exhale," KBW's Brian Slack said after the earnings release that First BanCorp beat analysts' expectations because of "stronger than expected net interest income," but "credit remains an issue." He maintained his "market perform" or hold rating on the shares with a 75-cent price target, and said his 2011 estimate of a net loss of 8 cents a share assumes "further capital plan execution."

### Balance Sheet

First BanCorp had \$16.7 billion in total assets as of September 30. Nonperforming assets - again including nonaccrual loans, loans past due 90 or more days and repossessed real estate - comprised 4.79% of total assets as of September 30, increasing from 4.59% in June and 3.21% in September 2009.

The tangible common equity ratio was 5.21% as of September 30, according to SNL Financial.

## Stock Ratios

The shares trade for 0.1 times tangible book value according to SNL.

## Analyst Ratings



Out of six analysts covering First BanCorp, one has a buy rating, four rate the shares a hold, and one analyst recommends investors sell the shares.

## 8. JPMorgan Chase

Company Profile

Shares of JPMorgan Chase closed at \$39.61 Friday, declining 8% over the previous year.

The company's loan loss reserves covered 4.95% of total loans as of September 30, while its net charge-off ratio for the first three quarters of 2010 was 3.50%.

## Income Statement

Net income for the third quarter was \$4.4 billion, or \$1.01 a share, compared to \$4.8 billion, or \$1.09 a share during the second quarter and \$3.6 billion, or 82 cents a share, during the third quarter of 2009.

JPMorgan's third-quarter provision for loan loss reserves was \$3.2 billion and loan loss reserves declined by \$1.68 billion during the third quarter, compared to a second-quarter reserve release of \$2.35 billion. This was a major factor in the link-quarter earnings decline.

Regarding risk from buybacks of nonperforming securitized mortgages, CFO Doug Braunstein said during the company's third-quarter conference call that "the functional equivalent of charge-offs, are going to remain high in 2011 and we've guided you to \$1 billion plus or minus. But eventually as we work through bad vintages, we would expect those actual costs to come down."

When asked about legal risks from the foreclosure mess, CEO Jamie Dimon said the company's \$4 billion in litigation reserves isn't tied specifically to mortgages and said the "lawsuits go on and class action suits and stock drop suits and Bear Stearns suits and WaMu suits... ain't going away," adding that "not all of those reserves were mortgage-related. They were related to other items we have to deal with as a company and we do try to be ahead of it."

About reserve releases, Dimon said "it's a silly post cyclical thing we go through, putting them all up and take them all down."

That being said, JPMorgan's loan loss reserve coverage is very strong, and if credit card delinquencies and losses continue to decline and the mortgage foreclosure debacle eases off over the next quarter, significant further reserve releases are in the cards.

### Balance Sheet

Total assets were \$2.1 trillion as of September 30 and the nonperforming assets ratio - including nonaccrual loans, loans past due 90 days or more and repossessed real estate - was 1.87%, declining from 2.06% the previous quarter and 1.99% a year earlier.

The net charge-off ratio for the third quarter was 2.75%, improving from 3.14% in the second quarter and 3.75% in the third quarter of 2009.

### Stock Ratios

The shares trade for 1.4 times tangible book value according to SNL Financial, and 8.6 times the consensus earnings estimate of \$4.62 a share for 2011. The forward P/E is just 7.3, based on the 2012 consensus earnings estimate of \$5.43 a share.

### Analyst Ratings

Analyst sentiment for JPMorgan Chase is quite strong, with 22 out of 25 analysts rating the shares a buy. The three remaining analysts recommend investors hold the shares. Based on the mean price

target of \$52.57 among analysts polled by Thomson Reuters, the shares have 33% upside potential.



## 7. Flagstar Bancorp

### Company Profile

Shares of **Flagstar Bancorp (FBC)** of Troy, Mich. closed at \$1.32 Friday,

down 82% from a year earlier.

Much of that decline followed the company's announcement on Oct. 27 of a \$380 million capital raise, which included 110 million new common shares priced at a dollar, which was a heavy discount to Flagstar's previous closing price of \$2.32. The company announced on Nov. 2 that it had raised a net \$385.8 million was making aggressive moves to trim its nonperforming loans, including the sale of \$474 million in problem mortgages and reclassification of another \$86 million as held-for-sale, for a total reduction of 84% of its nonperforming mortgages.

Flagstar also said that after completing the loans sales and transfers, its remaining \$106 million in non-performing first mortgages would be insured either by the Federal Housing Administration or the Department of Veterans Affairs.

Flagstar's ratio of loan loss reserves to total loans was 5.12% as of September 30 and its net charge-off ratio for the first three quarters of 2010 was 3.64%. The loan sale and associated write-downs will probably increase the net charge-off ratio for the fourth quarter, but the company's risk-profile will be greatly reduced.

### Income Statement

Flagstar reported a third-quarter net loss to common shareholders of \$22.6 million, or 15 cents a share, compared to a net loss of \$97 million, or 63 cents, in the second quarter and \$298.2 million, or \$6.36 a share, during the third quarter of 2009.

The provision for loan losses for the third quarter was \$51.4 million, declining from \$86 million the previous quarter and \$125.5 million a year earlier. The company released \$56 million in reserves during the third quarter.

The company reported improving mortgage origination volume of \$7.6 billion during the third quarter, rising 61% from the previous quarter.

After Flagstar's capital raise, Bose George of KBW lowered his net loss estimate for 2011 to two cents a share from 29 cents a share. He maintained his "market perform" or neutral rating on the shares but lowered his price target from five dollars to \$1.50 "on the reduced book value because of the capital raise."

### Balance Sheet

Total assets were \$13.8 billion as of September 30, and the company said that if its loan sales had been completed as of September 30, its nonperforming assets ratio would have been reduced to 4.33% from the actual 8.25%.

### Stock Ratios

Flagstar's shares trade for 0.6 times George's estimated tangible book value of \$2.21.

### Analyst Ratings



One out of four analysts covering Flagstar rate the shares a buy, while the other three analysts recommend investors hold the shares.

## 6. Zions Bancorporation

### Company Profile

Shares of **Zions Bancorporation** of Salt Lake City closed at \$21.36 Friday, rising 65% over the previous year.

The company's loan loss reserves covered 4.05% of total loans as of September 30, and the net charge-off ratio for the first three quarters of 2010 was 2.55%.

### Income Statement

Zions reported a third-quarter net loss to common shareholders of \$80.5 million, or 47 cents a share, compared to a second-quarter net loss to common shareholders of \$135.2 million, or 84 cents a share, and a loss of \$181.9 million, or \$1.43 a share, a year earlier.

The third-quarter provision for loan losses was \$184.7 million, declining from \$228.7 million the previous quarter and \$565.9 million during the third quarter of 2009. Net charge-offs totaled \$235.7 million during the third quarter, declining from \$255.2 million the previous quarter and \$381.3 million a year earlier.

Zions released \$26.5 million from loan loss reserves during the third quarter.

Loan originations totaled \$2.4 billion during the third quarter, increasing from \$1.8 billion during the second quarter. The net interest margin was 3.84%, compared to 3.58% the previous quarter and 3.91% in the third quarter of 2009.

### Balance Sheet

Total assets were \$51.1 billion as of September 30, and the nonperforming assets ratio was 4.76%, declining from 5.19% the previous quarter and 4.90% in September 2009.

Zions owes \$1.4 billion in TARP money. The company reported a Tier 1 leverage ratio of 12.00% and a total risk-based capital ratio of 16.54% as of September 30. The tangible common equity ratio was 7.03% and during the first three quarters of 2010 the company raised \$515.3 million in common equity, according to SNL Financial.

### Stock Ratios

The shares trade just above tangible book value, according to SNL. While the consensus among analysts polled by Thomson Reuters is for Zions to swing to a profit in the third quarter of 2011, Marty Mosby of Guggenheim said following the third-quarter earnings announcement that "ZION has now passed through the asset quality inflexion point for this cycle and will return to profitability by first quarter of 2011." Mosby also raised his target price to \$26 from \$25 and his 2011 EPS estimate to \$1.38 from \$1.32 and his 2012 estimate to \$3.98 from \$3.67.

### Analyst Ratings

Out of 27 analysts covering Zions Bancorporation, seven rate the shares a buy, 18 have hold ratings and two analysts recommend investors sell the shares.



## 5. PNC Financial Services

Company Profile

Shares of PNC Financial Services of Pittsburgh closed at \$56.64 Friday,

returning 5% over the previous year.

The company's ratio of loan loss reserves to total loans was 3.41% as of September 30 and its net charge-off ratio for the first three quarters of 2010 was 1.81%

### Income Statement

PNC reported third-quarter net income to common shareholders of \$1.1 billion, or \$2.07 a share, increasing from \$786 million, or \$1.47 a share, the previous and \$467 million, or a dollar a share, a year earlier.

Part of the earnings improvement was a \$128 million reserve release, as the third-quarter provision for credit losses was \$486 million, while net loan charge-offs totaled \$614 million. The company's high level reserve coverage when compared to its pace of charge-offs would make further significant releases appear likely over the coming quarters, although these could be partially offset by increases to litigation reserves in light of several mortgage-related lawsuits PNC discussed in its third-quarter 10-Q filing with the **Securities and Exchange Commission**.

In October, the **Federal Home Loan Bank of Chicago** sued several financial companies for rescission and other damages from \$3.3 billion in mortgage-backed securities purchases, "\$345 million of which was allegedly in transactions involving the National City entities." The FHLB is claiming the securities sales included misrepresentations and omissions, and PNC acquired the teetering National City in December 2008.

PNC's net interest margin for the third quarter was 3.96%, compared to 4.35% the previous quarter and 3.76% a year earlier. The decline in the margin from the previous quarter was attributed to weak loan demand and low interest rates.

Following the third-quarter earnings announcement, Richard Staite of Atlantic Equities maintained his "overweight" or buy rating for PNC, although he reduced his 2011 earnings estimate to \$5.79 a share from \$6.24 and his price target to \$66 from \$72, saying that "the key reason is a reduction in net interest income following updated guidance.

### Balance Sheet

PNC had \$260 billion in total assets as of September 30 and a nonperforming assets ratio - including nonaccrual loans, loans past due 90 or more days and repossessed assets - of 3.16%, improving from 3.38% the previous quarter and 3.50% in September 2009.

The Tier 1 leverage ratio was 9.92% and the total risk-based capital ratio was 15.55% as of September 30 and according to SNL Financial, the tangible common equity ratio was a strong 8.08%.

### Stock Ratios

The shares trade for 1.5 times tangible book value according to SNL and 10.1 times the consensus earnings estimate of \$5.63 for 2011 and just 8.8 times the \$6.44 estimate for 2012.

### Analyst Ratings

PNC is another name with strong analyst sentiment, as 22 out of 27 analysts covering the company



rate the shares a buy, while four analysts have hold ratings and one recommends investors sell.

### 4. BOK Financial

#### Company Profile

Shares of **BOK Financial**(BOKF) of Tulsa, Okla. closed at \$48.11 Friday,

returning 14% over the previous year.

The lender's ratio of reserves to loans was 2.69% as of September 30 and its net charge-off ratio for the first three quarters of 2010 was a relatively low 1.07%.

BOK Financial announced in its third-quarter 10-Q filing that it would merge all of its subsidiary banks into **Bank of Oklahoma, NA**, which would be renamed **BOKF, NA**. The company said the affiliates would continue to operate under their old names, but the consolidation would allow the company to make more efficient use of its capital.

BOK Financial also announced it had been named a defendant in three class action suits alleging "the manner in which the bank posted charges to its consumer demand deposit accounts breached an implied obligation of good faith and fair dealing and violates the Oklahoma Consumer Protection Act." While the company said that the amount ultimately claimed by the plaintiff who establishes a class representing all affected customers "could be material," BOK's "management anticipates the claims will be resolved without material loss to the Company."

### Income Statement

Third-quarter net income was \$64.3 million, or 94 cents a share, increasing from \$63.5 million, or 93 cents a share in the second quarter and \$50.7 million, or 75 cents a share, during the third-quarter of 2009.

The earnings improvement was fed by a reduction in the provision for loan losses to \$19.8 million during the third quarter from \$35.3 million the previous quarter and \$53.6 million a year earlier, although third-quarter earnings were hit by \$14.4 million in impairment losses.

Net charge-offs during the third quarter were \$20.1 million, for a small release in loan loss reserves.

The net interest margin for the third quarter declined to 3.50% from 3.63% in both the previous quarter and the third quarter of 2009, "as cash flows from [the company's] securities portfolio were reinvested at lower rates."

Following the earnings announcement, Brett Rabatin of Sterne Agee maintained his neutral rating on the shares but increased his 2011 earnings estimate to \$3.80 a share from \$3.77 and his 2012 estimate to \$4.55 from \$4.52 a share.

#### Balance Sheet

Total assets were \$24.3 billion as of June 30 and the nonperforming assets ratio was 1.55%, declining from 1.79% the previous quarter and 2.01% a year earlier. The third-quarter net charge-off ratio was 0.75%.

The Tier 1 leverage ratio was 8.61% and the total risk-based capital ratio was 12.30% as of September 30, and the tangible common equity ratio was 8.96% according to SNL Financia -- the highest among this group of banks.

BOK Financial did not participate in TARP.

#### Stock Ratios

The shares trade for 1.5 times tangible book value according to SNL Financial and 13.1 times the consensus earnings estimate of \$3.66 a share for 2011. The forward P/E drops to 11.2 based on the consensus earnings estimate of \$4.31 for 2012.

#### Analyst Ratings

Out of seven analysts covering BOK Financial, only one has a buy rating on the shares, while five have hold ratings and one recommends investors sell the shares.

With strong capital levels, continued profitability and improving asset quality, BOK Financial is a



lower-risk play among financials, although analysts are less than thrilled with the declining net interest margin.

### 3. Bank of Hawaii

#### Company Profile

Shares of Bank of Hawaii closed at \$44.49 Friday, up

4% over the previous year.

The company was featured as part of *TheStreet's* Best In Class series in October, as it was the only U.S. bank holding company to achieve returns on average equity exceeding 15% for the first half of 2010 and for each of the preceding five full years.

The shares have a dividend yield of 4.05%, based on a quarterly payout of 45 cents a share.

Loan loss reserves covered 2.76% of total loans as of September 30, while the net charge-off ratio for the first three quarters of 2010 was 1.12%.

#### Income Statement

Bank of Hawaii reported third-quarter net income of \$44.1 million, or 91 cents a share, compared to \$46.6 million, or 96 cents a share, the previous quarter and \$36.5 million, or 76 cents a share, a year earlier. Linked-quarter earnings decline was mainly attributed to "lower interest rates and lower loan balances." The net interest margin declined to 3.27% from 3.51% the previous quarter and 3.85% in the third quarter of 2009.

The third-quarter provision for loan losses was \$13.4 million, equaling net charge offs and declining from \$15.9 million in the second quarter and \$27.5 million in the third quarter of 2009.

Following the third-quarter earnings announcement, Joe Gladue of B. Riley & Co. upgraded his rating for Bank of Hawaii to a buy with a \$48 price target, although he lowered his 2011 earnings estimate to \$2.96 from \$3.44, saying "as the economy recovers, we expect the bank to achieve stronger EPS growth and to return funds to shareholders through stock buybacks and dividends."

#### Balance Sheet

Bank of Hawaii had \$12.7 billion in total assets as of September 30, and a nonperforming assets ratio of 0.44%, which was the same as the previous quarter, declining from 0.56% in September 2009.

The Tier 1 leverage ratio was 7.15% and the total risk-based capital ratio was 18.98%. The company's dividend is very well supported, with a payout ratio below 50% over the past four

quarters, and the tangible common equity was 7.95% as of September 30, according to SNL Financial. Bank of Hawaii did not participate in TARP.

## Stock Ratios

The shares trade for 2.1 times tangible book value according to SNL Financial and 15.2 times the consensus earnings estimate of \$2.92 for 2011 and 12.8 times the 2012 consensus earnings estimate of \$3.47 a share.

## Analyst Ratings

Out of 11 analysts covering Bank of Hawaii, four rate the shares a buy, while six analysts recommend



analysts hold the shares and one recommends investors sell.

## 2. Webster Financial

Company Profile

Shares of **Webster Financial** (WBS) of Waterbury, Conn. closed at \$17.25 Friday, returning

43% over the previous year.

The company's loan loss reserves covered 3.12% of total loans as of September 30 and its net charge-off ratio for the first three quarters of 2009 was 1.23%.

## Income Statement

Webster Financial reported third-quarter net income to common shareholders of \$17.8 million, or 22 cents a share, improving from \$12.7 million, or 15 cents a share, in the second quarter - which included a \$15.2 million gain on the sale of some of its investment in **Higher One** (ONE) -- and a net loss to common shareholders of \$26.1 million, or 39 cents a share, in the third quarter of 2009.

The main factor in the year-over-year earnings improvement was a reduction in the provision for loan losses, to \$25 million in the third quarter, from \$32 million in the second quarter and \$85 million in the third quarter of 2009. With third-quarter net charge-offs of \$28.7 million, the reserve release was \$3.7 million. During the company's third-quarter conference call, CFO Gerald Plus said "we would anticipate lower provisioning" during the fourth quarter.

Another bright spot for earnings was that net interest income before provisions for loan losses was \$134.7 million in the third quarter, increasing from \$132.3 million the previous quarter and \$126.7 million a year earlier. While many banks continued to report weak loan demand, Webster reported loan originations of \$644 million for the third quarter, increasing from \$579 million in the second quarter and \$225.8 million in the third quarter of 2009.

Following the earnings release, David Darst of Guggenheim Securities maintained his buy rating for Webster Financial, with a \$20.50 price target, citing "an improving fundamental outlook relative to the current valuation."

## Balance Sheet

Total assets were \$17.8 billion as of September 30 and the nonperforming assets ratio was 1.97%, improving from 2.03% the previous quarter and 2.27% a year earlier.

The Tier 1 leverage ratio was 8.83% and the total risk-based capital ratio was \$14.77 ad of September 30. According to SNL Financial, the tangible common equity ratio was 5.91%.

Webster owes the government \$200 million in TARP money, having already repaid \$200 million

## Stock Ratios

The shares trade for 1.3 times tangible book value according to SNL Financial and 18.2 times the consensus earnings estimate of \$95 cents a share for 2011. The forward P/E based on the consensus 2012 earnings estimate of \$1.36 a share is 12.7.

## Analyst Ratings



Out of 11 analysts covering the shares, three rate Webster Financial a buy, seven have hold ratings and one analyst recommends investors sell the shares.

## 1. Citigroup

Company Profile

Shares

of **Citigroup (C)** closed at \$4.29 Friday, returning 6% over the previous year.

The company's loan loss reserves covered 6.54% of total loans as of September 30, and Citigroup's net charge-off ratio for the first three quarters of 2009 was 4.59%.

According to SNL Financial, **Paulson & Co.** reduced its stake in the company from roughly 507 million shares as of June 30 to 424 million shares as of September 30.

SNL reported that according to master trust filings, Citigroup's 35+ days delinquency rate on credit cards declined to 4.74% at the end of October, from 4.93% the previous month and 5.67% a year earlier, although the company's annualized credit card loss rate of 10.27% in October was the highest among major U.S. card lenders.

## Income Statement

For the third quarter, Citigroup reported net income available to common shareholders of \$2.1 billion, or seven cents a share, compared to \$2.7 billion, or nine cents a share, in the second quarter and a net loss to common shareholders of \$3.2 billion, or 27 cents a share, during the third quarter of 2009.

The company's reserve release nearly equaled its earnings.

The provision for credit losses was reduced to \$5.9 billion during the third quarter from \$6.7 billion the previous quarter and \$12.1 billion a year earlier, with the company reporting a "a net release of reserves for loan losses and unfunded lending commitments of \$2.0 billion in the third quarter 2010, compared to a \$1.5 billion net reserve release in the prior quarter."

Following the earnings announcement, KBW's David Konrad said Citi's results were "a function of greater-than-expected reserve release," and while "Core revenues declined 5%," he raised his price target to \$5 from \$4.70 and his earnings estimate for 2011 to 32 cents a share from 21 cents a share.

Richard Staite of Atlantic Equities said in a report following the earnings announcement that "Management stated for the first time it sees the start of a capital return in 2012. We estimate a return to a 35% payout ratio would give investors a 6% dividend yield." State has an "overweight" or buy rating on the shares, with a \$6 price target.

## Balance Sheet

Citigroup had \$1.98 trillion in total assets as of September 30, with a nonperforming assets ratio of 1.67%, improving from 1.88% in June and 2.17% a year earlier. The third-quarter net charge-off ratio was 4.24%, declining from 4.78% a year earlier.

Citi's Tier 1 leverage ratio was 6.57% and its total risk-based capital ratio was 16.14% as of September 30. According to SNL, the tangible common equity ratio was 6.76% according to SNL Financial.

## Stock Ratios

The shares are still trading below book value according to SNL, and 9.3 times the consensus earnings estimate of 46 cents a share for 2011 and a low 7.8 times the consensus earnings of 55 cents a share for 2012.

## Analyst Ratings

Out of 20 analysts covering Citigroup, 10 rate the shares a buy, while eight have hold ratings and two analysts recommend investors sell the shares.

Past performance is not necessarily indicative of future results. The risk of loss in futures trading can be substantial no matter who is managing money. The opinion/comments of Yu-Dee Chang are not a recommendation or a solicitation to trade.