MORGAN-DEMPSEY
CAPITAL MANAGEMENT, LLC

Truist Financial Corp (TFC) | Initiate 1.50% **September 2022**

Company Overview

Truist Financial Corporation was formed by the combination of BB&T Corporation and SunTrust Bank in December 2019. It is the seventh largest U.S. Commercial bank that operates in a high-growth footprint (South/Mid-Atlantic) with select national businesses. Truist has a comprehensive and diverse business mix with distinct capabilities in insurance, investment banking, digital/point-of-sale lending, and wealth management. The firm operates through the following segments (Excluding Other, Treasury and Corporate (OT&C):

- Consumer Banking & Wealth (CB&W)
  - This segment is composed of Retail Community banking, Wealth, Mortgage Banking, Dealer retail Services, and National Consumer Finance.
  - CB&W generated approximately $12.102 Billion in Revenue and $3.235 Billion of net income in 2021, representing approximately 53.4% of sales and 40.4% of net income for the year (Excluding OT&C).
- Corporate & Commercial Banking (C&CB)
  - This segment is composed of Commercial Community Banking, Corporate & Investment Banking, Commercial Real Estate and Grandbridge. Grandbridge provides a wide range of services to the commercial and multifamily real estate markets.
  - C&CB generated approximately $7.81 billion in revenue and $4.261 in net income in 2021, representing approximately 34.5% of revenue and 53.2% of net income for the year (Excluding OT&C).
- Insurance Holdings
  - This segment is composed of Retail and Wholesale Insurance as well as Premium Finance. It provides property and casualty, employee benefits and life insurance to businesses and individuals. It also provides small business and corporate services such as workers compensation and professional liability as well as surety coverage and title insurance.
  - Insurance Holdings generated approximately $2.75 billion of revenue and $.508 billion of net income in 2021, representing approximately of 12.1% of revenue and 6.4% of net income (Excluding OT&C).

Transitional Strategy & Thesis

Truist management has taken longer than expected to integrate the BB&T and SunTrust operations. The teams behind the merger have used a “best-of-both” approach, selecting the “best” legacy products and systems from either SunTrust of BB&T for the combined operation. They also have used this time to upgrade systems when possible. While this resulted in higher-than-expected cumulative merger related costs of approximately $4 billion and a longer time frame, management believes that it produced the best platform for future growth.

With the integration process expected to be completed by the end of 2022, Truist management can now pivot from an integration mindset to an operating/growth mindset. The elimination of significant merger related costs combined with more than $1 billion in annualized cost savings should provide the company with a less complex narrative, improved earnings quality and additional capital that can be used for ongoing technology improvements, organic and inorganic growth investments, and capital return to shareholders.

We believe that TFC's insurance operations are an important differentiator for the firm. It is the seventh largest insurance brokerage in the world, is not tied to credit or rate cycles, and is a steady, strong cash generator. TFC continues to grow insurance primarily inorganically, making 11 acquisitions since 2019. The insurance business generated approximately 8.4% of TFC's 2021 operating income.

<u>Positives</u>

- Truist has a diverse business mix with distinct capabilities in insurance, investment banking, digital and point-of-sale lending, and wealth management. The company has a comprehensive product set that can be used to meet most or all its clients' needs.

- TFC is in an area of the country experiencing above average population growth, with 15 of its 20 largest markets growing faster than the overall US population.

- TFC has significant market share in its geographic footprint. It ranks among the top 3 banks in 17 of its top 20 markets

- One of the key drivers for the Truist merger was to have the scale to meet the increased need to invest in digital and innovation. The company showed its commitment to continual digital improvement when it opened its Innovation &Technology Center in Charlotte at the end of 2021. Truist will partner directly with clients, innovators, digital product managers, designers, engineers, fintech firms, and partner vendors at the Center to develop new digital products and services to meet client needs. Tech investment spend, approximately 70% operational/30% transformational in 2021, is expected to be 55% operational and 45% transformational in 2023.

- Truist is investing in its Payments business to enable convenient commerce and strengthen its capabilities. This could be an interesting area or growth. It is growing this business through multiple channels including

    - Digital payments across all client segments
    - Wholesale payments using an integrated cash management platform that provides intuitive client experiences
    - Point-of-sale lending (basically a small one-time installment loan made at checkout that has a fixed, generally short term, fixed payment schedule.

<u>Negatives & Risks</u>

- While the company sells at approximately 1.1 times book value, it also trades at approximately 2.4 times tangible book value. The goodwill generated by the merger-of-equals as well as the bolt-on acquisitions of insurance brokerages and smaller fintech firms are the drivers of this differential. While we believe that the acquisitions behind the goodwill will provide a long-term benefit for the company, the price-to-tangible book value is at an elevated level.

- Additional expenses could be incurred if currently unidentified integration issues are uncovered during the final stages of the merger of equals.

- The potential for a stricter regulatory environment, particularly for the large super-regional banks, could negatively impact TFC's profitability.

- Weakness in the economy could result in lower loan volumes and a decline in credit quality in the loan portfolio.

- Higher short-term rates should increase the cost of funds and the currently inverted yield curve will pressure the profitability of new loans.

Current & Historical Valuations

Valuation Matric	Current	5-Year High	5-Year Low	Average	Vs. Industry
Price to Earnings (PE)	10.7	20.9	6.5	14.5	.9
Forward PE	9.1	15.8	5.8	12.4	.9
Price to Expected Growth (PEG)	1.4	92.3	.6	5.3	1.2
Price to Book Value	1.1	1.7	.5	1.3	.8
Price to Tangible Book Value	2.4	2.7	.9	2.2	1.3
Dividend Yield	4.4%	7.1%	2.2%	3.3%	1.9%

Note:

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