

The objective of this report is to utilize public accessible information to analyze, interpret, and estimate the fundamental value of the Bank of America Corporation's stock (from 1/1/02 through 4/27/03), with the purpose of drawing a recommendation as to hold, buy, or sell based on the current stock price.

Introduction

Meet the machine we know as The Bank America Corporation. It is a product of one of the largest bank mergers in history when Nations Bank fused with Bank America on September 30, 1998. During its short life, Bank of America has fulfilled its inevitable fate as the nation's first coast-to-coast bank. The 3rd largest bank in the US (assets), behind Citigroup and J.P Morgan Chase, also possesses the nation's most extensive branch network, with more than 4,200 locations spanning over 21 states while employing 133,900 people. It operates in about 30 other countries, and controls an investment bank subsidiary; Banc of America Securities. Bank of America Corporation is classified in the Money Center Bank Industry while it trades on the NYSE under the ticker BAC. The firm's total market capitalization (4/27/03) is \$109.04 billion which is categorized as a "Large Cap" firm and total assets of \$660,458.

Stock Performance

To begin analyzing BAC's stock performance precisely, observe the stock price beginning at the start of the year 2000 through the present (4/25/03).

Chart # 1 – (MSN Money: BAC chart)

Chart 1 displays the stock performance of the Bank of America Corporation over the specified period ultimately increasing. There appears to be a consistent pattern (somewhat) in that the stock price seems to peak during the middle of the year and fall during the later stages of the year. The stock price also seems to be on a rebound period from the year-end 2001 where the stock reached as low as \$40.00. The volume graph (below) does not seem to have an obvious pattern although the data may become usual later in the analyses.

To continue, please observe the Bank of America's stock performance relative to the S&P 500 and the leading competitor JP Morgan and Chase (from 1/1/03 till 4/25/03).

Chart # 2 – (MSN Money: customized BAC chart)

Chart 2 illustrates Bank of America's (black) stock performance in percentage terms relative to the S&P 500 (yellow) and BAC's top competitor, J P Morgan Chase (red). Interpreting the historical chart we see Bank of America's stock has been outperforming not only the S&P 500 Index but its larger competitor as well. The firm appears to have a support level at approximately -20% and a resistance level at +60% during the period presented (or range).

To proceed, let us examine the performance of the Banking industry as a whole compared to the performance of Bank of America's stock. Let us observe Bank of America's beta – the measure of how sensitive the security's return is to overall market movements. The beta for BAC is 1.35 while its market beta is 1.0. This infers that BAC's stock has 35% more risk than that of the market average, which isn't that bad.

Chart #3 – (Smartmoney.com)

Chart 3 illustrates the relationship between Bank of America Corporation's stock (blue), the industry average (black), and the DJIA (grey). The exhibit shows that the BAC stock and the industry average are very positively correlated. This allows us to assume when the industry as a whole is increasing so will the Bank of America Corporation's stock price. In contrast, when the market is doing bad so will the Bank of America Corporation.

	Company name	Symbol	Year
Value	Bank of America	BAC	2002
Value	Actual		Expected

Efficiency Ratio <60% 73.61%
 [Compares Non-Interest expenses to Total Income]

ROA (Return on Average Assets) - ROI [Net Income / Average Total Assets]	>1	1.4
ROE (Return on Average Equity) [Net Income / Avg. Shareholders' Equity]	>15%	18.9%
Capital Adequacy (Capital Ratio) [Total Stockholders Equity / Total Assets]	>8-10%	7.62%
Provision for Loan Losses as a % of Total Loans [Provision for Loan Losses / Total Investment loans]	Curr. Yr. <1%	.0152 = .2%
Net Interest Margin	>5%	4.8%
Interest Rate Spread	>3%	4.2%
Nonperforming assets as a percent of total assets [Nonperforming Assets / Total Assets]	<1	.82
Types of loans -- Risk based upon the type of loans made.	>33%	46%

Evaluating Key Measures

The following is a spreadsheet completed to view and analyze the key measures of the Bank of America Corporation's risk and profitability. Note: compare to expected values or benchmark values to those of BAC's.

- The efficiency ratio – BAC's value is higher than that the benchmark, which is not good. If the ratio increases, then the company is losing a larger percentage of its income to expenses, which is essentially bad for the bank.
- The ROA – BAC's ROA is performing better than benchmark, which represents how much money made for every dollar of assets held. Small ROA's represent big profits because banks are so highly leveraged.
- The ROE – BAC's ROE is also outperforming the expected benchmark. This represents how much money made for every dollar of equity invested.
- The Capital ratio – BAC's capital ratio is falling a little short of the expected value. The ratio describes the percentage of total assets in shareholders equity. Due to the industry in which Bank of America operates this is an understandable shortcoming.
- The Provision of loss as percentage of Total loans – BAC's has a value of 0.2%, which is exceptional. The value expresses the amount of loan loss (default) occurred relative to total loans in percentage terms.
- The Net Interest Margin – BAC's net interest margin falls short of the benchmark value. The net interest margin is the difference between interest paid to depositors (other source of funds) and the interest collected on loans and other investments. This is a key measure of a bank's success in the basic banking business environment.

Bank of America's Strategic Initiatives

Bank of America Corporation is competing to bring higher standards into the core of the financial service's present and future innovations. Things such as the new "palm scanner" for safety deposit boxes, the new mini Check Card that attaches to key chains, or the new digital check imaging system that provides copies of checks to customers online. The Bank of America Corporation also focuses on continually improving innovations that drive internal growth, or "human capital". That is why is 2002, 58000 associates nationwide attended productivity and quality training.

Bank of America's Risk Management

There appear to be four major risks that the Bank of America Corporation is exposed to. One, credit risk or the risk that contractual cash flows (loans or securities) may not be paid by a customer or business to BAC in full. This risk is not company specific, in that every financial institution bears this type of risk. Two, BAC is exposed to liquidity risk. This is the risk that a sudden surge in liability withdrawals may leave Bank of America in a position of having to liquidate assets in a very short period of time and at low prices (relative to market value). Liquidity risk is typically an industry specific risk, in that it only affects institutions that have asset and liability maturities. Three, the Bank of America Corporation must bear market risk. This is the risk incurred when asset and liability values fluctuate with the changes in interest rates, exchange rates, and/or market prices. Last in a risk that affects businesses across all scopes, operational risk. This is the risk that occurs due to the potential loss in the firm resulting from processes, technology, legal issues, reputation, and/or execution or regulation of business policies. The fundamental value of BAC

For this section of the analysis I have chosen to use the constant growth rate model in which a firm assumes that it will grow at a specified rate constantly through time. I used the dividend growth rate from the MSN money website to input into this dividend discount model.

So, $V_0 = D_0(1+g)/(k-g)$ - - - -or- - - - $V_0 = D_1/(k-g)$

We assume: $g = (P/E)/(PEG) = 11.5/1.20 = 9.6\%$, $D_0 = \$0.64$ last quarter dividend and...

(CAPM) $K = (R_f + \text{Stock Beta}) \times (K_M - R_f) = (.0125 + .90) \times (.13 - .0125) = .10612$ or 10.6%

Therefore: $V_0 = \$0.64(1+.10)/(.106-.096) = \70.40

This model appears to have undervalued the Bank of America Corporation's stock, which is currently trading at \$76.67. Another reason of deviation is that the stock may possibly be overvalued in its current state and the value stated may be the true fundamental value. Bank of America's P/E ratio is currently 11.5, which show evidence of the "value" in this firm. Many investors tend to avoid stocks with high P/E ratios because they may appear to be overpriced. BAC's stock price is undervalued with a relative low P/E, which makes this firm attractive to many investors.

In conclusion, I recommend that an investor that is looking for a highly valued company with low risk, to buy this stock. The company has strength in its current and future financial position and contains a strong foundation in its profitability. Although BAC has surpassed its primary opportunity for growth, its fundamental data surpasses most industry benchmarks.

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