

# *Financial Services Alert*

Volume 4 - 1

**The Elite Five in Massachusetts Finance:  
Performance of the Largest Massachusetts  
Financial Services Firms in Recent Years**

**Part 1: State Street Corporation**



**Foreword by Arindam Bandopadhyaya  
Director, Financial Services Forum  
College of Management, UMASS-Boston**

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**SECTION I: Foreword**  
**Arindam Bandopadhyaya**  
**Director, Financial Services Forum**  
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With days like in which the Dow Jones Index experienced an intra-day 600-point swing, the financial markets roller coaster ride since the beginning of this year is becoming a bit too bumpy. Most observers expect that markets will remain choppy and uncomfortable for anyone with a low appetite for volatility.

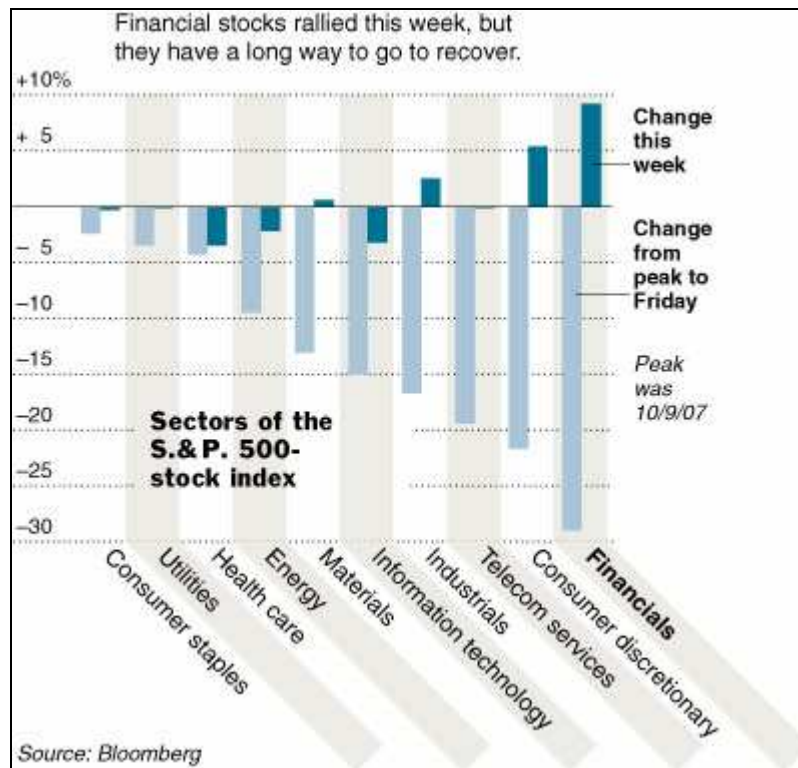
The sub-prime mortgage crisis, accompanied by the bursting of the real estate bubble and high price of oil, has led to market declines since they posted record highs in the summer of last year. While almost all sectors have been adversely affected, the financial sector has been hit particularly hard (please see Exhibit 1).

By January 23, 2008, led by financial giants like Citigroup, Merrill Lynch CEOs of which resigned within weeks of each other, and Morgan Stanley, financial institutions have recognized sub-prime related losses or write-downs in excess of \$130 billion. A more complete list of affected firms is in Exhibit 2.

The *Financial Services Forum* thought that this is an opportune time to examine the financial services sector in Massachusetts in some detail. Financial services play a very critical role in Massachusetts; 32% of private services provided in the Commonwealth is due to financial activities (please see Exhibit 3 for a detailed breakdown). The five largest public financial firms, by market capitalization, listed in the Massachusetts Bloomberg Index are State Street Corporation, Enterprise Bancorp, Wainwright Bank, Boston Private Financial Holding and Independent Bank Corp. In a three-part series of the *Alert*, the *Forum* presents an in-depth analysis of each of these firms. In the first part of this series, we examine the State Street Corporation. Beginning with a general overview, we provide an examination of the financial ratios and equity price, an analysis of the Strengths, Weakness, Opportunities and Strengths and a scrutiny of the Economic Value Added of the firm. The remaining four firms will be studied in two subsequent releases of the *Alert*.

Happy reading and stay tuned!

**Exhibit 1**  
**Percentage Returns in Sectors of the S&P 500 Index,**  
**October 9, 2007 - January 18, 2008**



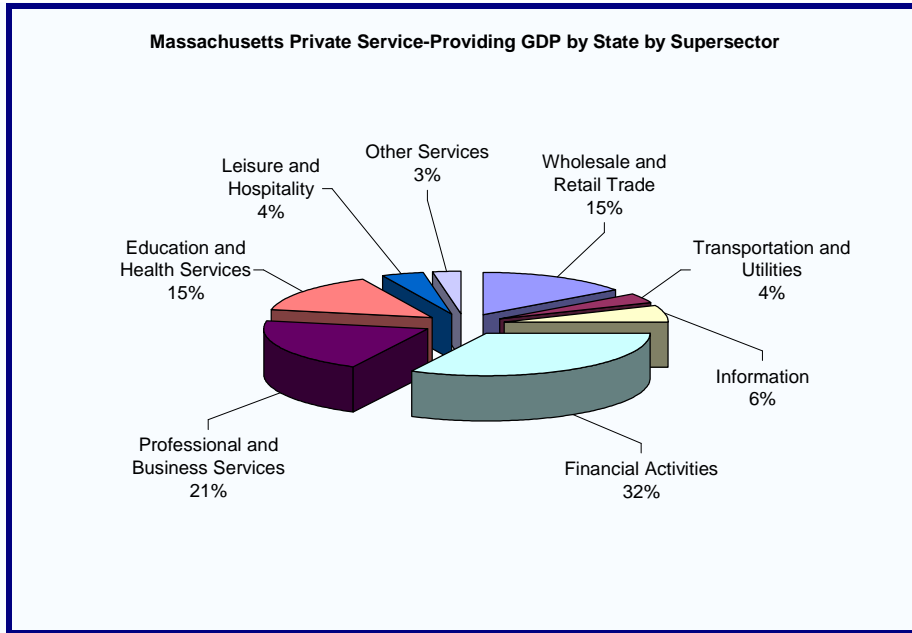
Adapted from the *New York Times*, January 23, 2008

**Exhibit 2**  
**Sub-Prime Mortgage Crisis Related Losses and Write Downs**  
**as of January 23, 2008**

<b>Company</b>	<b>Business Type</b>	<b>Loss (Billion)</b>
Citigroup	Investment bank	\$24.1
Merrill Lynch	Investment bank	\$22.5
UBS AG	Investment bank	\$13.7
Morgan Stanley	Investment bank	\$10.3
Crédit Agricole	Bank	\$4.8
HSBC	Bank	\$3.4
Bank of America	Bank	\$5.28
CIBC	Bank	\$3.2
Deutsche Bank	Investment bank	\$3.1
Barclays Capital	Investment bank	\$2.7
Bear Stearns	Investment bank	\$2.6
RBS	Bank	\$2.6
Washington Mutual	Savings and loan	\$2.4
Swiss Re	Re-insurance	\$1.07
Lehman Brothers	Investment bank	\$2.1
LBBW	Bank	\$1.1
JP Morgan Chase	Investment bank	\$2.9
Goldman Sachs	Investment bank	\$1.5
Freddie Mac	Mortgage	\$3.6
Credit Suisse	Bank	\$1.9
Wells Fargo	Bank	\$1.4
Wachovia	Bank	\$3.0
RBC	Bank	\$0.360
Fannie Mae	Mortgage	\$0.896
MBIA	Bond insurance	\$3.3
Hypo Real Estate	Investment bank	\$0.580
Ambac Financial Group	Bond insurance	\$3.5
Commerzbank	Bank	\$0.427
Société Générale	Investment bank	\$3.0

Source: Wikipedia

### Exhibit 3 Massachusetts Private Service-Providing GDP by State by Supersector



Source: Bureau of Economic Analysis

## EXECUTIVE SUMMARY

### **State Street Corporation**

- Financial holding company organized under the laws of the Commonwealth of Massachusetts, established in 1986
- The company is among the top providers of mutual fund and pension processing and custody services

### **SWOT:**

#### **Strengths:**

- Dominant Market Position
- Strong customer relationships
- Robust Top line Growth.

#### **Weaknesses:**

- High Susceptibility to market volatility
- High susceptibility towards interest risk and lending risk

#### **Opportunities:**

- Increasing demand for Insurance and Pensions plans in the UK
- Opportunities in Investment Banking
- Growing opportunities in Investment Banking
- Positive Outlook for the global asset management market

#### **Threats:**

- High Interest rates worldwide
- Financial Markets Risk

#### **Financial Ratios as compared to Industry:**

- Low Debt to Capital ratios in the last ten years
- Very high receivable turnover ratio which means higher cash collection ability as compared to the industry
- Higher Gross Profit Margin ratios means highly efficient as compared to competitors
- Higher Return on equity for the last ten years and higher Return on Assets for most of the period
- Earnings per share (EPS) is far below the industry standards for the past four years.
- Higher P/E ratio, showing growth expectation by investors

#### **Shareholder Return:**

- Company stock listed on NASDAQ
- For the five year period the HPR for state Street is 38% while for the same time period the HPR for market (S&P 500) is 57%

**EVA:**

- Calculated for the last eight years
- Positive EVA for through out the given time period with positive EVA momentum for last three years.
- Positive and growing EVA spread which shows that company is in a good condition and the Return on Capital is greater than the Cost of Capital

### State Street (NYSE: *STT*)

1 Lincoln St.  
 Boston, MA 02111  
 United States  
 Phone: 617-786-3000  
 Fax: 617-664-4299

#### Key Information:

<b>D-U-N-S Number</b>	062156427
<b>SIC Code</b>	Primary SIC: 6022 – State commercial banks Secondary SIC: 6712 – Bank holding companies 6282 - Investment Advice
<b>NAICS Code</b>	Primary NAICS: 522110 – Commercial Banking 551111 – Offices of Bank Holding Companies <a href="#">52393, 52393 (hoovers)</a>
<b>Company Type</b>	Public - NYSE: <i>STT</i> Headquarters
<b>Year Of Founding or Change In Control</b>	1986
<b>State of Incorporation</b>	MA
<b>Key Numbers</b>	
<b>Fiscal Year-End</b>	December
<b>2006 Sales (mil.)</b>	\$9,525.0
<b>1-Year Sales Growth</b>	27.1%
<b>2006 Net Income (mil.)</b>	\$1,106.0

<b>1-Year Net Income Growth</b>	32.0%
<b>2005 Employees</b>	20,965
<b>1-Year Employee Growth</b>	6.6%

## COMPANY OVERVIEW

State Street Corporation is a financial holding company organized under the laws of the Commonwealth of Massachusetts, and through its subsidiaries, provides a full range of products and services for institutional investors worldwide. The company is among the top providers of mutual fund and pension processing and custody services; its target clients include large-scale institutional investors and corporations who can choose from a service menu that includes accounting, foreign exchange, cash management, securities lending, and more.

State Street operates in about 25 countries spanning 100 markets worldwide. Its key markets are US, Australia, Belgium, Canada, Cayman Islands, Chile, France, Germany, India, Japan, China, South Africa, Taiwan, Thailand, UAE and the UK. Its State Street Global Advisors (SSgA) unit performs asset management services. Boston Financial Data Services, a partnership with DST Systems, provides shareholder services to clients. Another joint venture, CitiStreet (with Citigroup), manages retirement and pension plans.

At the vanguard of financial services technology, State Street is banking on its computerized analytical and organizational tools to woo and retain clients. Offerings include foreign exchange trading platform FX Connect and Global Link, which provides market research and portfolio analysis. The company boosted its foreign exchange offerings with the announcement in January 2007 of the definitive agreement to acquire Currenex.

In February 2007, the company announced a definitive agreement to acquire Investors Financial Services Corp., or “Investors Financial”, a \$12 billion bank holding company based in Boston. Under the terms of the agreement, the company will exchange 0.906 shares of its common stock for each share of Investors Financial common stock. The acquisition is expected to close in the third quarter of 2007.

One of the world's largest managers of institutional accounts (which represent much of State Street's approximately \$1.75 trillion of assets under management), the company is also at the top of the custody-services heap (particularly in the US and key European markets), with assets under custody of \$11.85 trillion at year end 2006.

Company reports two lines of business: Investment Servicing and Investment Management. Given Co.'s services and management organization, the results of operations for these lines



of business are not necessarily comparable with those of other companies, including companies in the financial services industry.

i) Investment Servicing provides services for U.S. mutual funds, collective investment funds worldwide, corporate and public retirement plans, insurance companies, foundations, endowments, and other investment pools. Products include custody, accounting, daily pricing and administration; master trust and master custody; recordkeeping; foreign exchange; securities finance; deposit and short-term investment facilities; loans and lease financing; investment manager and hedge fund manager operations outsourcing; and performance, risk and compliance analytics to support institutional investors. Co. provide shareholder services, which include mutual fund and collective investment fund shareholder accounting, through 50%-owned affiliates, Boston Financial Data Services, Inc. and the International Financial Data Services group of companies.

ii) Investment Management offers an array of services for managing financial assets, including investment management and investment research, primarily for institutional investors worldwide. These services include passive and active U.S. and non-U.S. equity and fixed income strategies, and other related services, such as securities finance.

## **HISTORY**

The US's chaotic post-revolutionary era gave birth to the first ancestor of State Street Corporation. Union Bank was founded in 1792 by Boston executives, breaking the eight-year monopoly held on Boston banking by Massachusetts Bank (a forerunner of FleetBoston, which was acquired by Bank of America in 2004). Governor John Hancock's distinctive signature graced Union's charter; the bank set up shop at 40 State Street near the port and enjoyed the glory days of New England's shipping trade.

In the mid-19th century, Boston's financial eminence faded as New York flexed its economic muscle. In 1865 the bank was nationally chartered and changed its name to National Union Bank of Boston. It got a new neighbor in 1891: Directors of Third National Bank set up State Street Deposit & Trust to engage in the newfangled business of trusts.

In 1925 National Union Bank merged with State Street and inherited its custodial business. The bank grew through the 1950s; acquisitions included the Second National Bank and the Rockland-Atlas National Bank.

In 1970 State Street converted to a holding company -- the State Street Boston Financial Corp. (State Street Boston Corp. as of 1977). The company also went international that decade, opening an office in Munich, Germany.

Soaring inflation and the recession of the 1970s forced the company to radically rethink its mission. The 1974 passage of the Employee Retirement Income Security Act changed the laws governing the management of pension funds and created an opportunity. State Street was one of the first banks to move aggressively into high-tech information processing, and

affiliate Boston Financial Data Services began servicing pension assets in 1974.

Encouraged by that success, in 1975 new CEO William Edgerly (who served until 1992) steered State Street away from branch banking and into investments, trusts, and securities processing. An early achievement was designing PepsiCo's retirement plan. Fee-based sales approached 50% of revenues; the company could now quit focusing on lending. In the 1980s and 1990s the company built its administration and investment management businesses overseas and moved into software.

Evolving in the late 1990s, State Street left non-core businesses but expanded globally. In 1997 it formed European Direct Capital Management to invest in eastern and central Europe. State Street Global Advisors opened a London office to serve wealthy individuals outside the US in 1998.

The company sold its commercial banking business to Royal Bank of Scotland in 1999, signaling an exit from that business and narrowing State Street's scope to the asset and investment management businesses. The company also bought Wachovia's custody and institutional trust business and teamed with Citigroup to sell 401(k) retirement products.

In 2000 State Street created FX Connect, an electronic foreign exchange trading system. Also that year David Spina took over as CEO from the retiring Marshall Carter.

The firm bought Bel Air Investment Advisors and its broker/dealer affiliate Bel Air Securities in 2001 to cater to the ultra wealthy. In 2003 State Street sold its corporate trust business to U.S. Bancorp and its private asset management business to Charles Schwab's U.S. Trust. Spina retired in 2004; his protégé, Ron Logue, stepped in as chairman and CEO. The company was reappointed as the financial advisor for the \$2.4 billion Suffolk County (New York) Council Pension Fund in 2007.

## **PRODUCTS AND SERVICES ANALYSIS**

The company recorded income from continuing operations of \$1.1 billion, a 16% increase from \$945 million for 2005. Total revenues increased 15% from 2005, and return on equity from continuing operations was 16.2%.

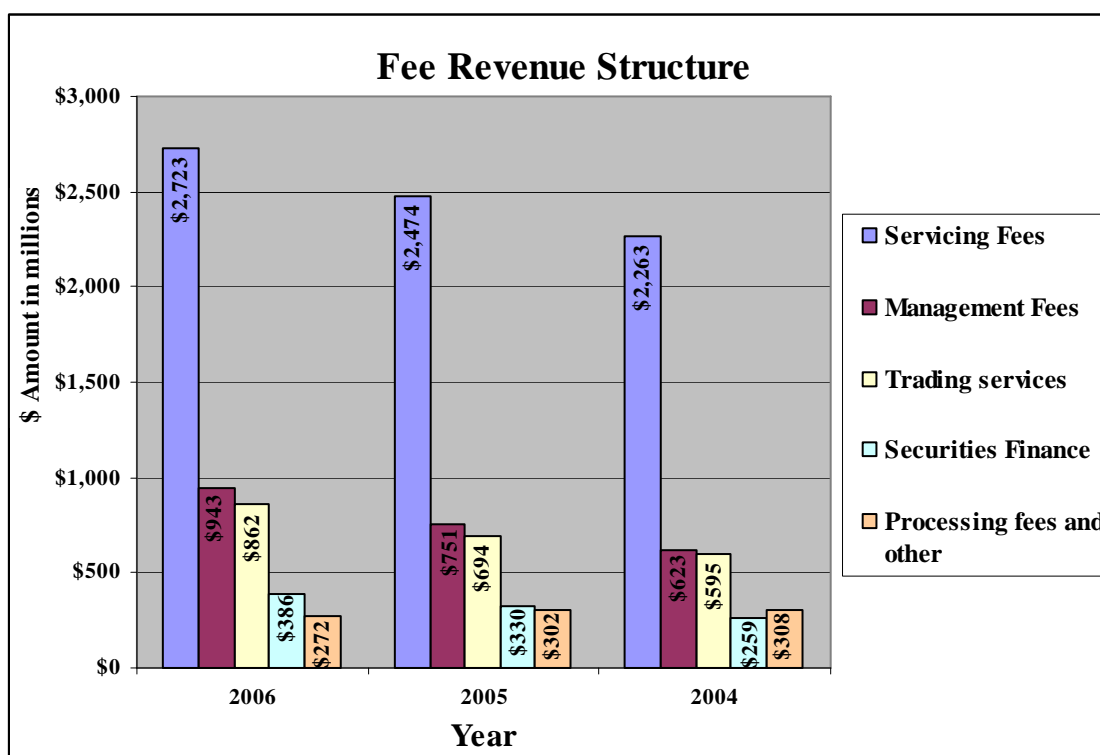
### ***Revenues categorization***

#### ***- Fee Revenue:***

Servicing and management fees are the largest components of fee revenue, and collectively comprised approximately 71% of total fee revenue for 2006 and 2005. These fees are a function of several factors, including the mix and volume of assets under custody and assets under management, securities positions held and the volume of portfolio transactions, and the types of products and services used by customers, and are affected by changes in worldwide equity and fixed income valuations.

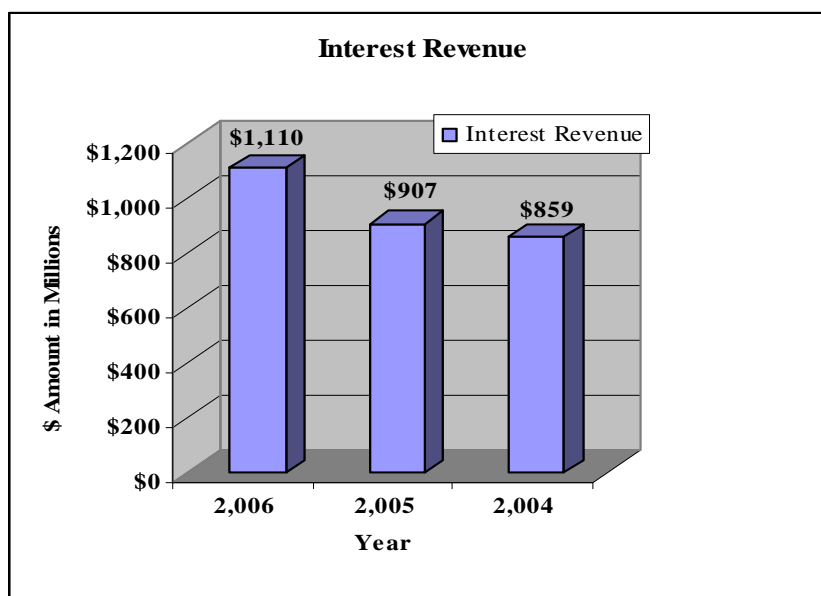
The 14% increase in total revenue from 2005 was primarily driven by increases in servicing and trading services fees and securities finance revenue, as well as a 19% increase in net interest revenue, slightly offset by a decline in processing fees and other revenue.

Servicing fees were up from 2005 due to net new business from existing and new customers, higher equity valuations and higher customer transaction volumes. The increase in trading services revenue reflected a higher dollar volume of foreign exchange trades for customers and a higher volume of fixed income transition management business. Processing fees and other revenue declined from 2005, partly as a result of a decline in fees from Deutsche Bank AG as GSS customer deposits were converted to our systems.



- ***Interest Revenue***

Interest revenue for 2006 increased by 19% from 2005 due to an increase in average interest-earning assets, as well as higher yields on the investment securities portfolio.



### ***Revenues by Geography***

Company continues to expand its business outside of the U.S., particularly in Europe and the Asia Pacific region. For 2006, approximately 43% of the consolidated revenues were generated from non U.S. activities, up from approximately 39% for 2005 and at year end 2006 company employed 8,630 outside the US.

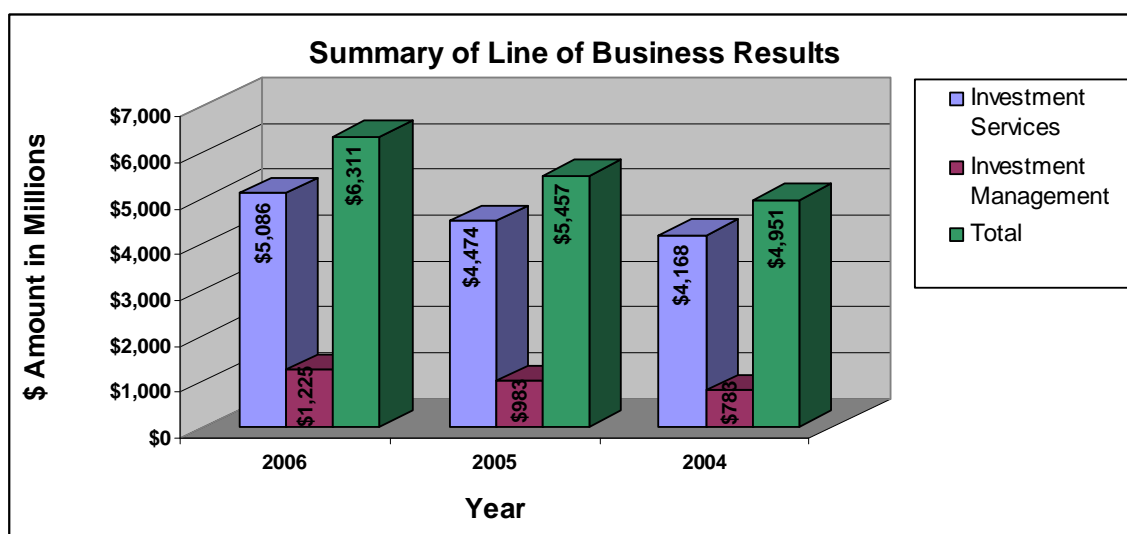
### **SWOT ANALYSIS**

#### **Strengths**

- ***Dominant Market Position:*** State Street is one among the leading players in the mutual fund custody and accounting services in the US. The group is involved in calculating more than 31% of the US mutual fund prices provided to NASDAQ. With a 37% market share, State Street has a leading position in the market for servicing US tax-exempt assets for corporate and public pension funds. State Street provides trust and valuations services for more than 4,500 daily priced portfolios, making it the leader for both monthly and daily valuation services.

The group's global custodian network spans more than 100 geographic markets. State Street provides custody services for more than 20% of fund assets in Canada. In Germany, the group provides its services for more than 19% of retail and institutional fund assets. In the UK, it provides custody services for 19% of pension fund assets and provides administration services to more than 21% of mutual fund assets. The group provides its services to more than 10% of the hedge fund market. As of December 31, 2006, the company had total assets of \$107.35 billion, total deposits of \$65.65 billion, total shareholders' equity of \$7.25 billion and employed 21,700. The group's strong market position gives it a competitive advantage.

- ***Strong Customer Relationships:*** State Street has built a reputation of providing superior quality products and services that has enabled it to bag repeat mandates. For example, Halliburton's multinational pension plan (comprising approximately \$6 billion in assets) renewed its contracts with State Street after more than ten years of relationship. In April 2006, the group expanded its relationship with Illinois-based Calamos Investments to provide fund accounting services for nine open-end mutual funds and one variable insurance fund representing nearly \$29.8 billion in assets. These strong relationships provide State Street with strong investor confidence as well as guaranteeing repeat and word-of-mouth business.
- ***Robust Top line growth:*** The group has recorded a strong top line growth over the past few years. From 2005 to 2006, State Street's revenues recorded a growth of 15.3%. This was driven by strong divisional performance. For the same period the group's business divisions including investment servicing and investment management recorded growth of 13.7% and 24.6%, respectively. A strong top line growth implies that the group has strengthened its market position which gives it's a competitive advantage.



- ***Acquisitions of Complementary business and technologies:*** The Company's deployment of dedicated resources for the development of strategic alliances and divestitures of portions of its business, in addition to fostering organic growth opportunities, are an active part of company's overall business strategy to remain competitive.

### Weaknesses

- ***High Susceptibility to market volatility:*** Lower market volatility, even in a generally rising market environment, may reduce trading volumes of company's

customers, and the ability to achieve attractive spreads, which could lead to lower trading revenues.

## Opportunities

- ***Increasing demand for Insurance and Pensions plans in the UK:*** In the UK, old age population is rapidly growing and has more than trebled as a percentage of total population over the last century. To meet demographic pressures long-term healthcare spending in the UK is likely to rise by around 315% in real terms between 2000 and 2051. This would mean higher spending by aged people in UK. This along with the gradual withering of the value of the state pension indicates higher demand of other saving instruments like insurance and private pensions. The group won four mandates (in 2005) to service the pension funds of four local authorities in the UK; when combined have a total assets of about £1.7 billion. This would enable the group to realize greater revenues going forward.
- ***Growing opportunities in Investment Banking:*** The global investment banking industry is benefiting from the increasing consolidations, mergers, acquisitions, corporate reforms and restructuring initiatives. The number of corporate deals has been rising strongly in US and Asia Pacific region. Corporations across geographies have been considering mergers and acquisition strategies to realize cost synergies against mounting oil prices; increased competition, pricing pressures, gap in product mix and asset concentration. The increased demand for investment banking products may ensure continued growth of the group's investment servicing division which would boost its total revenues.
- ***Positive Outlook for the global asset management market:*** The global asset management and custody banks industry had an asset base of \$49,157 billion in 2005, representing a compound annual growth rate (CAGR) of 8% for 2001-2005. Moreover, in the year 2010, the global asset management and custody banks industry is likely to reach a value of about \$68,210.3 billion, an increase of about 39% since 2005 and US is the most significant region, contributing 52.4% of global assets. The CAGR of the industry during the period 2005-2010 is expected to remain at 6.8%. The main factors driving this growth would include the need for private individuals to make provision for their pension requirements. The group's asset under management has increased at a CAGR of 36.4% over the period 2003-2005. This growth seems set to continue over the next few years driven by strong demand for asset management services.

## Threats

- ***High Interest rates worldwide:*** The past few years have seen Central Banks impose higher interest rates to check inflation and the over heating of regional economies. The US Federal Reserve has led the way raising interest rates for the

17th consecutive time on June 29, 2006 to 5.25%. The Bank of England raised interest rates to a high of 4.75% in UK. The European Central Bank (ECB) also raised interest rates to 3%. In periods of rising interest rates, the group's investment management business would be under pressure as changes in the earned rates on the related invested asset portfolios tend to lag behind market rates. In a period of rising interest rates, institutional investors may redeem shares in money market funds to invest in direct securities offering higher yields. These redemptions in turn would reduce managed assets, thereby reducing group's fee revenue. If the interest rates continue to rise, it may put pressures on the group's profitability.

- **Financial Markets Risk:** Financial markets around the world have been volatile in 2006 after robust earnings over the past few years. Most of the financial markets seem to be going through a phase of correction. On May 19, 2006 European shares suffered their worst weekly points drop since July 2002, as worries over inflation and falling commodity prices affected equity markets. In the week ending May 19, 2006 all the three major market indices in the US lost significantly with the Dow Jones industrial average losing 2.1%, (its worst week in four months), the S&P 500 losing 1.9% and the NASDAQ composite losing 2.2%. The emerging markets have seen the greatest volatility with major indexes in Russia, India and China recording record intra-day losses. Between May 9 and June 13 (2006), Brazil's Bovespa fell 29.6% accompanied by India's Sensex recording a 32.4% fall. If the volatility of the global financial markets continues, it can result in investors engaging more actively in selling, leading to a return of the bear market. This could result in a decline in the group's revenues.
- **Consolidation in the Global Financial Services Industry:** Consolidation in the global financial services sector appears, set to continue in the US, Europe and Germany. A number of large commercial banks, insurance companies and other broad-based financial services firms have merged with other financial institutions to diversify their offerings and reduce their corresponding business risks. On the back of their enhanced size and competitive position, these institutions aim to increase their market share and make the most of scale economies, which could result in pricing and margin pressure for the group in some product markets.

### **Financial Ratio Analysis**

In this section, we have performed the conventional financial statement analysis of State Street Corporation. We have analyzed the last ten years of data to have a better and more accurate understanding of the company's performance. In general an examination of a company's financial ratios over a longer period will depict a more accurate picture of its health because it balances out large divestitures, stock repurchases, changes in accounting systems and economic fluctuations that tend to skew the numbers.

The Exhibit's under Appendix - A gives the snapshot of financial position of State Street's in comparison to the industry values over a period of last ten years. To simplify and

facilitate the industry average calculations, we have used the Standard and Poor's "COMPUSTAT- financial application" wherein the NAICS codes were used for the industry reference.

There are a total of five hundred and fifty one companies including States Street under the respective NAICS code. We did come across some difficulties wherein the data for a couple of companies wasn't available. So as to accomplish the most accurate results the correction/adjustments were made in our calculations. Also note that despite the existence of outliers every value is included in the calculation of the average.

For convenience sake, the ratios to be examined are divided into five categories. These categories are related to the aspect of the company's performance to which they relate and also to their input values; these five ratios are Short Term Solvency Ratios, Long Term Solvency Ratios, Asset Management or Turnover Ratios, Profitability Ratios and Market Value Ratios.

### ***1) Short Term Solvency Measures***

This includes the Current and Quick Ratio. These ratios, as their name depicts relate to the ability of the firm to generate cash in the short term, the liquidity of a company's assets. These ratios have little or no significance in the context of Financial Institutes / Companies. So in the absence of any significant financial data availability for these two ratios, we are unable to provide any insight on the company's short term solvency position.

### ***2) Long Term Solvency Measures***

The second set of ratios examines a firm's ability to meet its long term obligations. The long-term debt to capital ratio relates total long-term debt to total capital giving an investor a greater insight at the firm's long term solvency situation.

As can be seen in Exhibit 1 that the Total debt to capital ratio for State Street is higher than the industry average for all years over the span of last one decade, the gap between the Company's and Industry widens the most from 1999 to 2001 i.e. during the IT boom period. Whereas the Long term Debt to Capital ratio valuation indicates the lower values for all year over the period of same last one decade. This statistics leads us to the exploration of very fine observation that the company has a substantial amount of short term debt in order to leverage the maximum benefits out of the highly volatile and ever changing business world.

### **3) Asset Management Ratio**

The first of these ratios is the receivables turnover ratio, which is used to quantify a firm's effectiveness in extending credit as well as collecting debts. It is calculated by dividing Net sales with Receivable ( $\text{Net Sales} / \text{Receivables}$ ). The greater the number of times receivables turn over during the year, the shorter the time between sales and cash

collection. The value of the ratio for the company is way ahead of the industry average of 0.2, which is a favorable factor that reflects organization's ability to collect cash from its sales and thus sustain liquidity position.

The other ratio of this set is the total asset turnover ratio, which relates value of sale and total assets. It is calculated by dividing Net Sales with the average of the current and prior year's total assets. The results obtained here for both the company and the industry are pretty close to each other. Over the last decade starting from 1996; as depicted in Exhibit-4 we can see a downward trend in the asset turnover ratio value till 2003 and since then there has been a consistent increase (growth) in it.

#### **4) Profitability Ratio**

These ratios demonstrate how well a firm is utilizing their assets or equity to create income and wealth and how efficiently selling is done. One of these ratios i.e. Gross Profit Margin represents the percentage of each sales dollar remaining after a firm has paid for its cost of producing goods/services. It is calculated by dividing gross income (profits) by net sales. The gross profit tells an investor the percentage of revenue / sales left after subtracting the cost of goods sold/services. A company that boasts a higher gross profit margin than its competitors and industry is more efficient. Clearly the State Street completely outperforms the industry average over the whole time period covered in our analysis. The industry average has always stood below the reported value for State Street in all the respective years of our analysis time period.

Return on equity, ROE, measures a firm's ability to leverage its equity for profitability. State Street posted an encouraging ROE numbers and greatly outperformed the industry. The company reported a highly positive and favorable ROE figures during the last decade i.e. of 1996-2006, touching a maximum value of 23.34. Though the company ROE has been highly volatile, but the good news is that it has always been above the industry average. Return on assets for State Street is closely aligned to the industry value.

#### **5) Market Value Ratios**

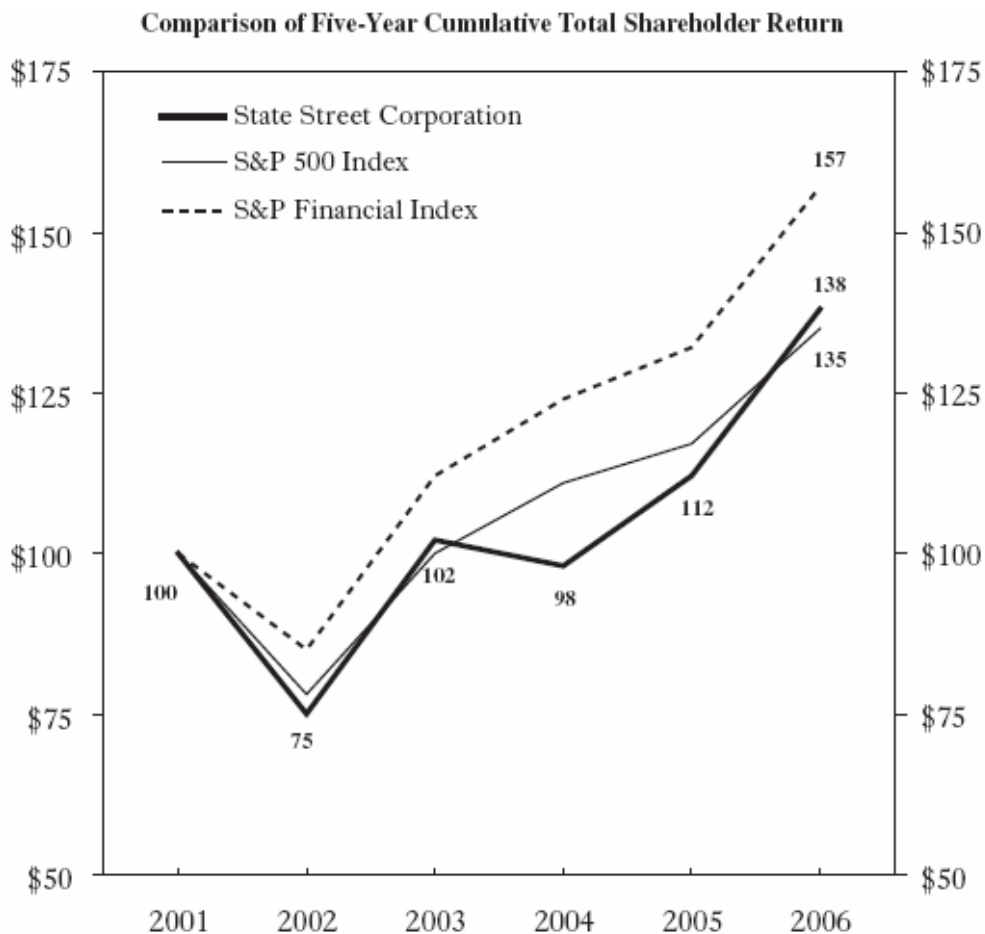
Last but not the least we have Market Value Ratios, which include earnings per share, EPS, and price to earnings, P/E. The measures relate net income and outstanding shares, and price per share with EPS respectively. They give information regarding the valuation of the company's stock, and thus the company itself, by the market, analysts, and investors in particular. Earnings per share represent basic earnings per share before extraordinary items and discontinued operations. Here the company has underperformed the industry EPS value. The company's EPS has average around 2.0 over the last decade. Though the industry average has observed a steep growth especially from 2003 – 2005, but the good news is that we have very close and promising neck to neck results for the company and the industry.

On the P/E front in order to have a better and clear picture we computed the same on the monthly basis by dividing the month end close price with the appropriate 12-months

moving earnings per share. If the most recent earnings per share figure were not available then the close price was divided by the sum of the previous quarter's value of 12-month moving earnings per share. Both the industry and company's P/E value has been highly volatile, and since the beginning of year 2003 we can see the values for each other closely related as depicted in exhibit-9 and as of year 2005 its been averaged around a value of 20.

## SHAREHOLDER RETURN PERFORMANCE PRESENTATION

The graph presented below compares the cumulative total shareholder return on State Street's common stock to the cumulative total return of the S&P 500 Index and the S&P Financial Index for the five fiscal years, which commenced January 1, 2002 and ended December 31, 2006. The cumulative total shareholder return assumes the investment of \$100 in State Street's common stock and in each index on December 31, 2001 and assumes reinvestment of dividends. The S&P Financial Index is a publicly available measure of 88 of the Standard & Poor's 500 companies, representing 25 banking companies, 23 insurance Companies, 26 diversified financial services companies, and 14 real estate companies. (State Street – Annual Report 2006).



## EVA Analysis:

Economic Value-Added Analysis measures the amount of value a company has created for its shareholders. It determines how much profit a company has produced after it has covered the cost of its capital. Whereas conventional accounting methods deduct interest payments on debt, Economic Value-Added Analysis also deducts the cost of equity—what shareholders would have earned in price appreciation and dividends by investing in a portfolio of companies with similar risk profiles. Economic Value-Added Analysis thus offers a truer picture of the return a company delivers to its shareholders and provides a framework to assess options for increasing it. By making the cost of capital visible, Economic Value-Added Analysis helps companies identify whether they need to operate more efficiently, to focus investment on projects that are in the best interests of shareholders and to work to dispose of or reduce investment in activities that generate low returns.

The basic formula is:

$$\text{EVA} = (\text{ROC} - \text{COC}) * C = \text{NOPAT} - \text{COC} * C$$

Where

$$\text{ROC} = \frac{\text{NOPAT}}{C}; \text{ called the return on capital employed.}$$

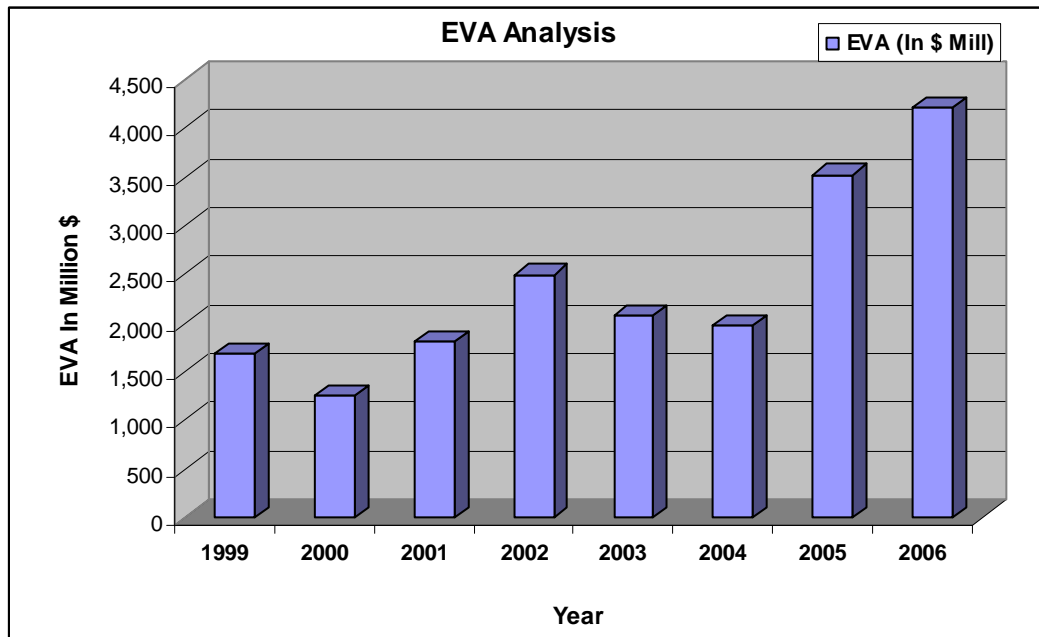
ROC: Return on capital.

COC: Weighted average cost of capital.

NOPAT: Net Operating Profit after Tax

C: Capital employed

**Note:** For EVA calculation, all the financial figures have been obtained from [mergenetonline.com](http://mergenetonline.com). In order to calculate the current assets; the results reported for current ratio and current liabilities were inputted in the formula: Current Assets = Current Ratio x Current Liabilities. The values for Long term debt, Equity and operating margin were taken from [valueline.com](http://valueline.com).

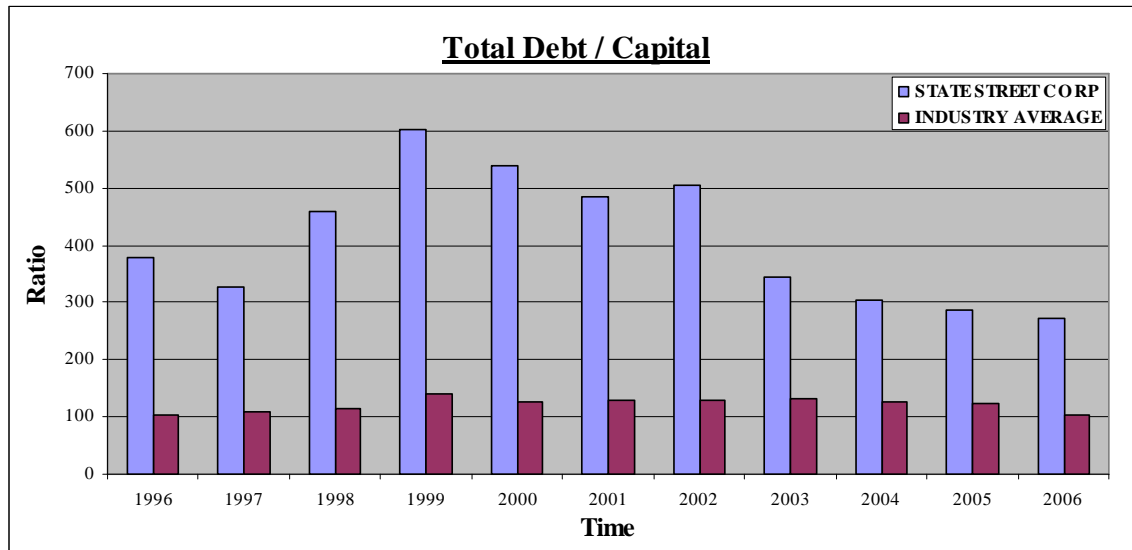


As depicted in the figure above, the EVA for State Street has been volatile. During the boom period the company reported a continuous growth in its EVA and only during the recession and afterwards it showed a decline in the EVA for almost two years. But the good thing is that the initiatives and strategic planning done during that period is paying now by as depicted by the drastic jump in the EVA in year 2005 relative to previous five year period. Also the results for the year 2006 are quite promising.

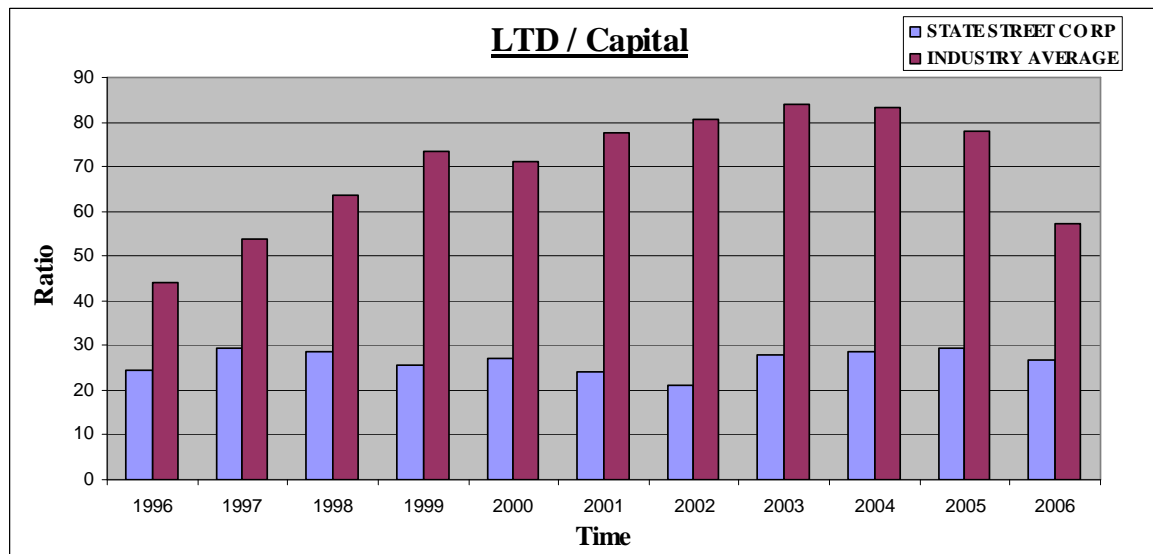
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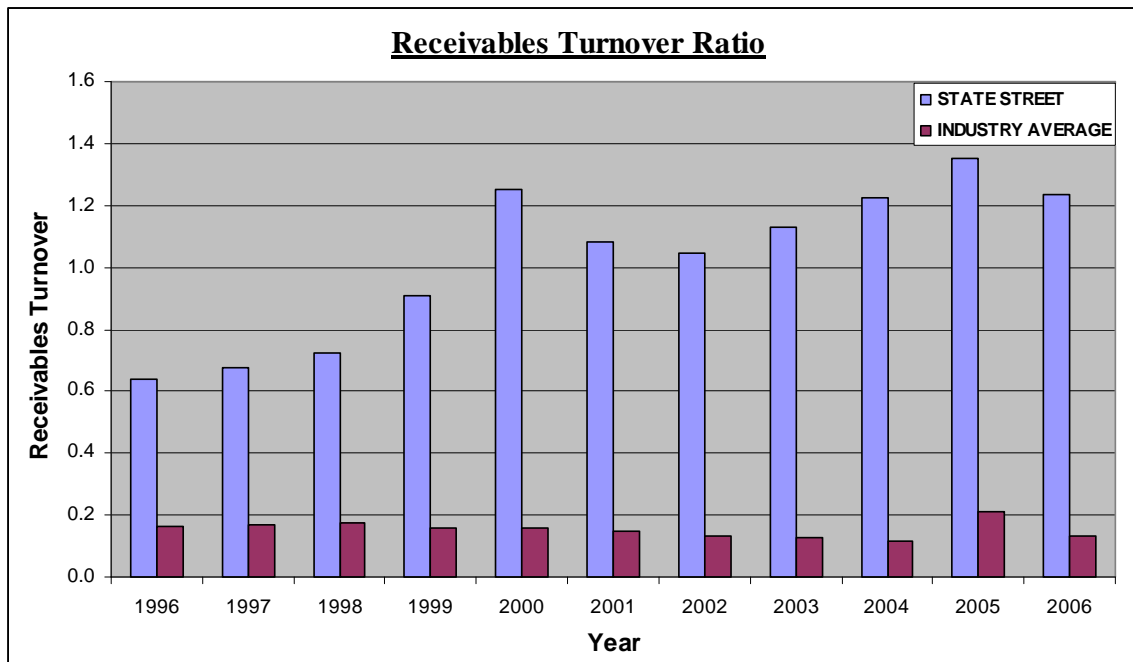
**Appendix-A:**



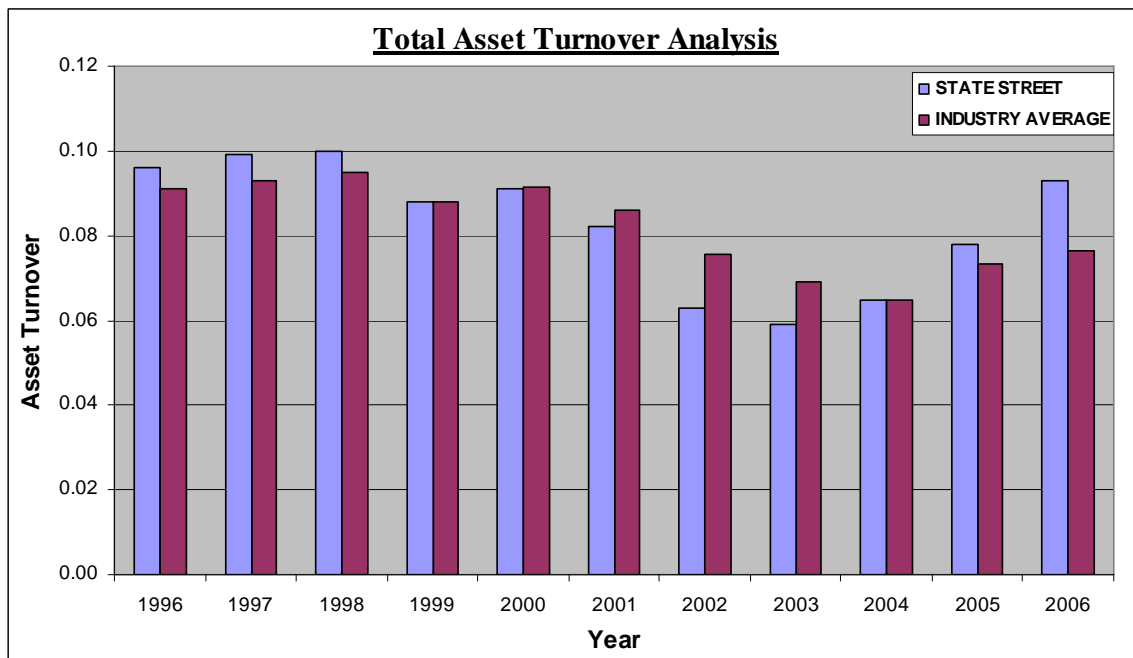
**Exhibit-1**



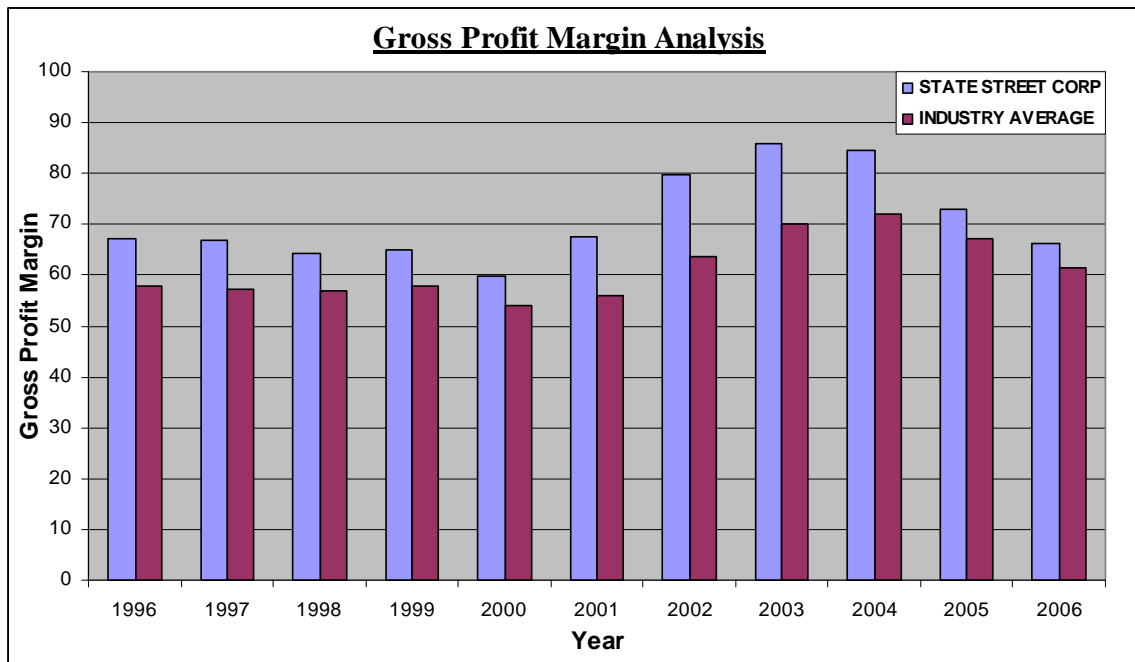
**Exhibit-2**



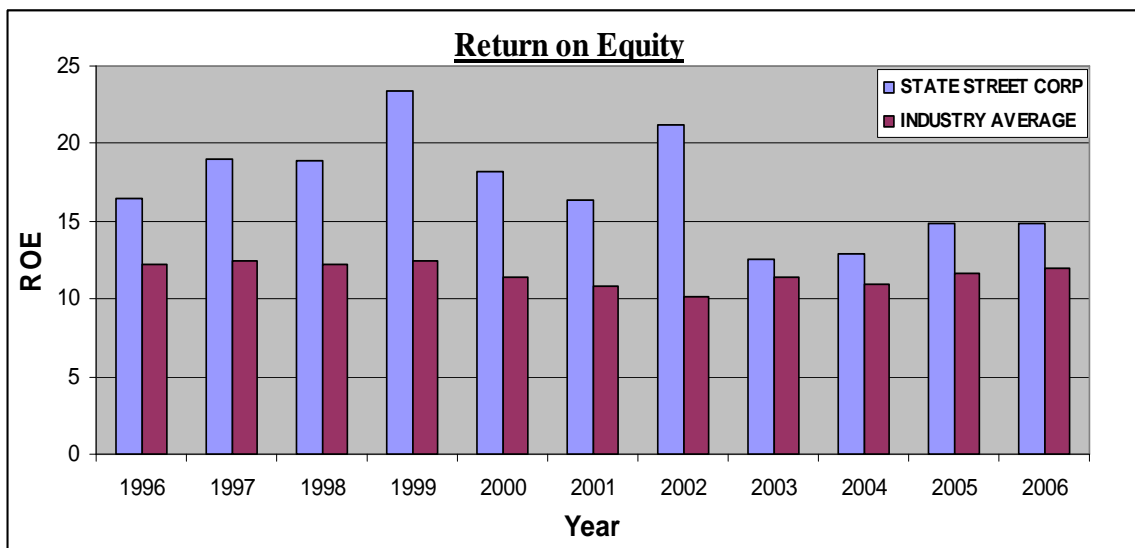
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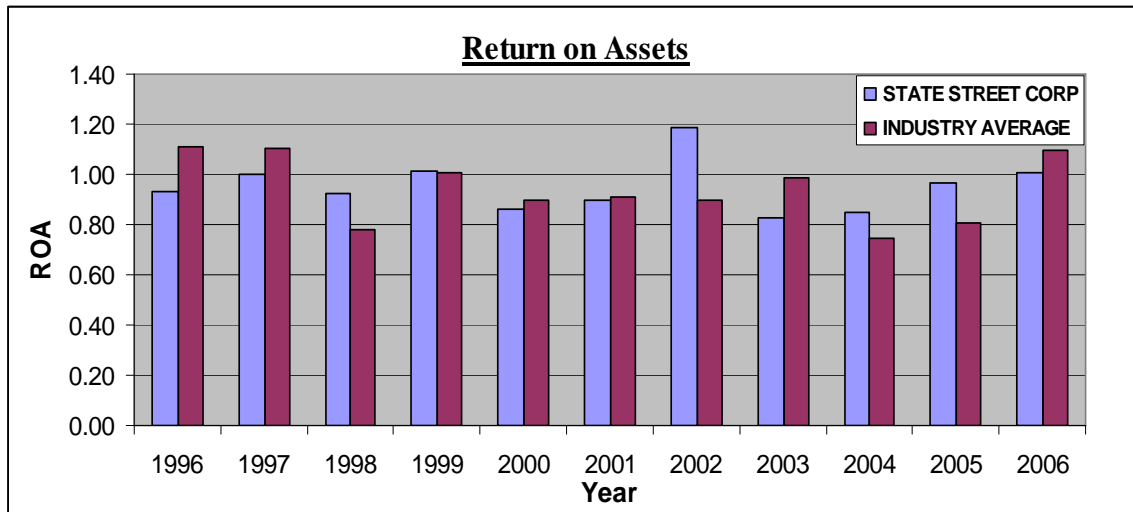
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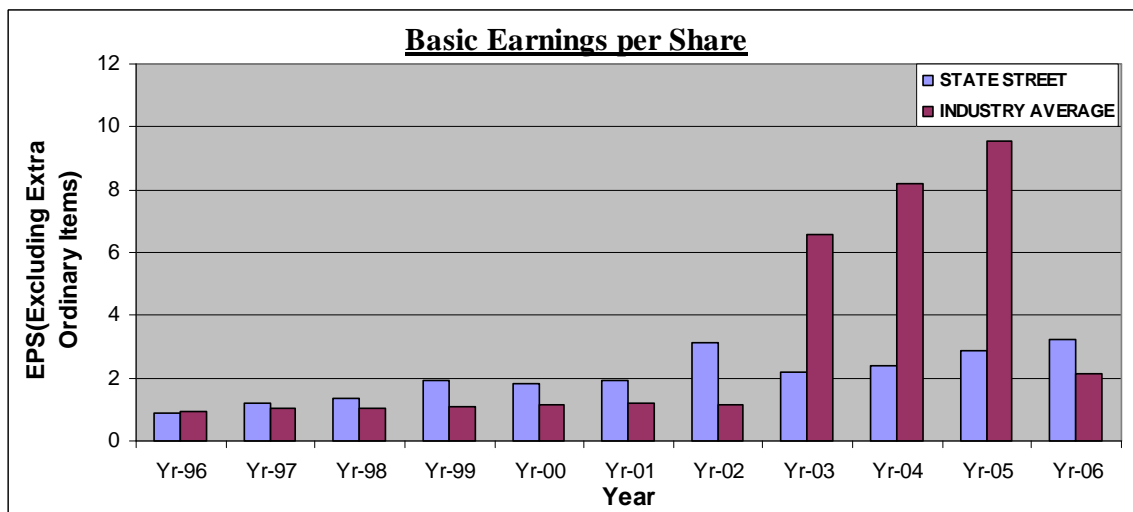
**Exhibit-5**



**Exhibit-6**



**Exhibit-7**



**Exhibit-8**

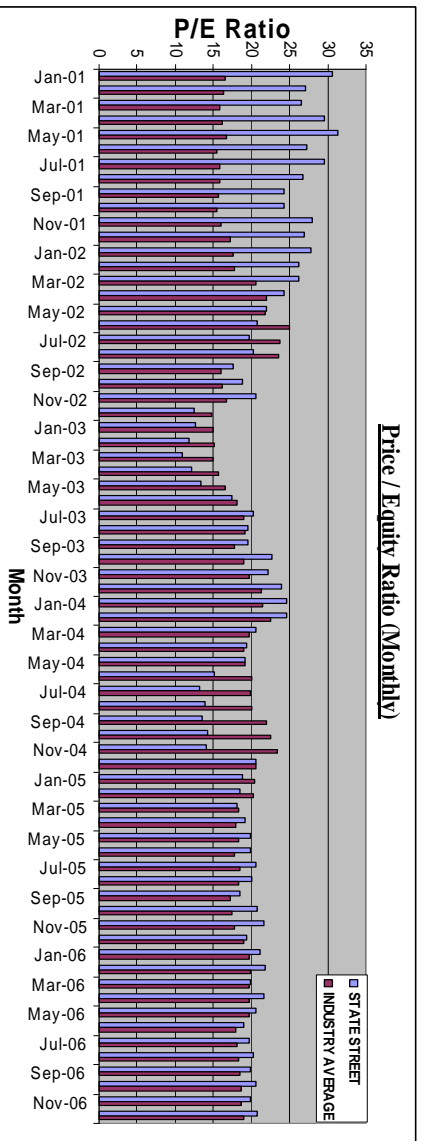


Exhibit-9