TITAN CAPITAL MANAGEMENT RESEARCH REPORT FOR: **TCM BOND**

Analyst(s): Ngoc Nguyen Date: October 24, 2022

COMPANY/TICKER: **ALLY FINANCIAL 8.00% 11/01/2031** **Bond** **Sell**

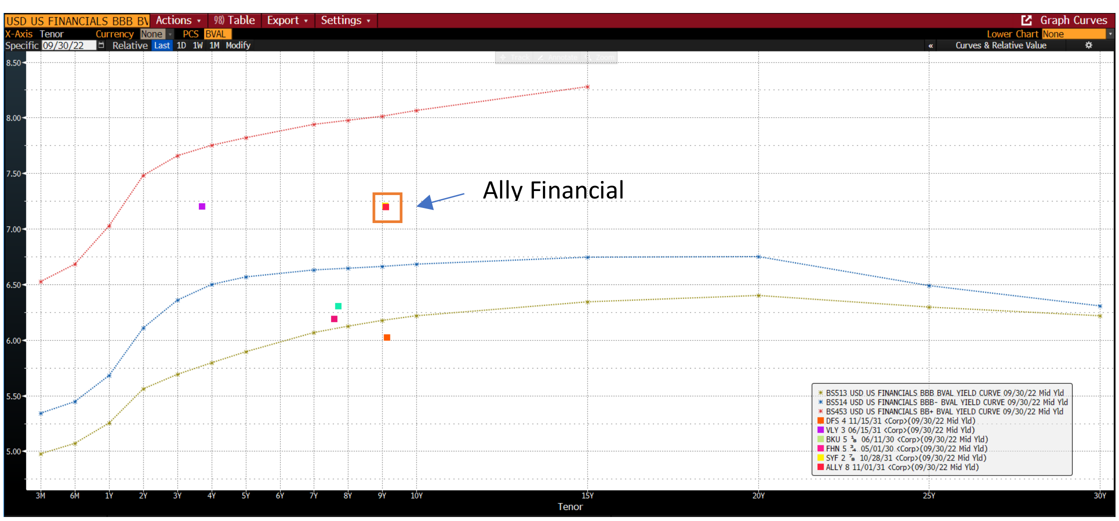
EXECUTIVE SUMMARY

The TCM Bond team recommends a Sell of Ally Financial Inc. 8.00% 2031 bond [370425RZ5] to allocate the proceeds to higher credit quality securities and different duration. Ally Financial is a financial company with a high concentration in the composition of automotive loans, which may carry higher risk during an economic slow-down. The company's pre-tax income from continuing operations declined $317 million year over year for Q2 2022. Ally financial reported a profit miss for Q3 2022 with net income of $272 million compared to $683 million a year ago. The company's higher net financing revenue was offset by higher provision for credit losses, noninterest expense, and lower other revenue. The company issued a warning in October 2022 that the Net Charge-Off (NCOs) rate will likely continue to climb from 0.2% in Q3 2021 to 0.85% in Q3 2022. Ally Financial bond is rated Baa3/BBB-, offers a yield-to-worst of 7.77%, 352 bps OAS (Treasury), and a 6.127-year duration. While risk-rewards trade-off appeared fairly attractive, the TCM bond team believes that it would be more prudent to focus on stable assets rather than chasing high yields in the current economic environment. The Ally Financial bond have an above average probability of suffering from headwinds such as:

1. The possibility of a decline in consumer spending big-ticket financing purchases in a rising rates environment.
2. Ally Financial low Altman Z-score indicates that the company carries higher credit risk which may impact the bond's price significantly if its rating decline from BBB- to BB+.
3. High Total Debt/EV (71.4%) and negative FCF yields (-5.35%) may indicate the firm is highly levered and may not have sufficient cash flow to satisfy its future obligations.
4. NCOs in retail auto sales quadrupled from $108 million in Q2 2022 to $257 million in Q3 2022 which is likely to continue to climb in a slowing economy.

Key uncertainties: The economic environment may not suffer too badly from an economic slow-down. Probability of missing out on the potential yields that we can earn should the economy strengthen. Overall TCM bond portfolio's current duration is 65% of the benchmark, sell of Ally Financial will further reduce duration of the portfolio.

CUSIP	Price @ 10/24/2022	Coupon	YTM	YTW	OAS (Trsy)
	$ 101.88	8.00%	7.77%	7.77%	352
370425RZ5	**Duration**	**Credit Rating**	**Seniority**	**Offered Amt.**	**Amt. Outstanding**
	6.127	Baa3/BBB-	Sr. Unsecured	$ 4,000,000	$ 493,742



COMPANY OVERVIEW

Ally Financial, Inc. is a holding company, which provides digital financial services to consumers, businesses, automotive dealers, and corporate clients. The company was founded in 1919 and is headquartered in Detroit, MI. It generates Operating Income through the following segments: 1) Automotive Finance Operations (83.7%), 2) Insurance Operations (8.5%), 3) Mortgage Finance Operations (0.8%), and 4) Corporate Finance Operations (7.0%).

- The Automotive Finance Operations segment offers retail installment sales contracts, loans and leases, offering term loans to dealers, financing dealer floorplans and other lines of credit to dealers, warehouse lines to companies, fleet financing, providing financing to companies and municipalities for the purchase or lease of vehicles and equipment, and vehicle remarketing services.
- The Insurance Operations segment focuses on finance protection and insurance products sold primarily through the automotive dealer channel, and commercial insurance products sold directly to dealers.
- The Mortgage Finance Operations segment consists of the management of a held-for-investment consumer mortgage finance loan portfolio, which includes bulk purchases of jumbo and LMI mortgage loans originated by third parties.
- The Corporate Finance Operations segment provides senior secured leveraged cash flow and asset-based loans to mostly United States based middle market companies focused on businesses owned by private equity sponsors with loans typically used for leveraged buyouts, mergers and acquisitions, debt refinancing, restructurings, and working capital.

Source: FactSet Fundamentals

Table 1: Condensed Financial Data

	JUN '22	MAR '22	DEC '21	SEP '21	JUN '21	MAR '21	5-yr. Avg.
Revenue	8,776	7,537	7,375	6,829	7,009	7,206	7,455
Growth	*16.44%*	*2.20%*	*8.00%*	*-2.57%*	*-2.73%*		*4.27%*
EPS (diluted)	$6.93	$7.95	$8.20	$8.22	$7.60	$5.83	$7.45
Growth	*-12.73%*	*-3.08%*	*-0.31%*	*8.22%*	*30.39%*		*4.50%*
Dividends per Share	$1.10	$0.99	$0.88	$0.82	$0.76	$0.76	$0.89
Growth	*11.11%*	*12.50%*	*7.32%*	*7.89%*	*0.00%*		*7.76%*
Net Interest Margin	3.95%	3.93%	3.80%	3.56%	3.42%	3.16%	3.64%
Growth	*0.51%*	*3.42%*	*6.74%*	*4.09%*	*8.23%*		*4.60%*
Return on Risk-Weighted Assets	1.27%	1.76%	1.80%	2.03%	2.59%	2.29%	1.96%
Growth	*-28.00%*	*-2.19%*	*-11.65%*	*-21.47%*	*12.98%*		*-10.07%*
Cash & Secs/Deposits (M)	24.49%	25.19%	25.69%	25.78%	26.57%	26.12%	25.64%
Growth	*-2.74%*	*-1.95%*	*-0.38%*	*-2.98%*	*1.74%*		*-1.26%*
Net Charge-Offs / Average Loans	0.12%	0.11%	0.09%	0.05%	-0.01%	0.10%	0.08%
Growth	*12.42%*	*24.25%*	*82.30%*	*984.54%*	*-105.30%*		*199.64%*
Non-Performing Loans/Total Loans	1.07%	1.11%	1.17%	1.12%	1.14%	1.27%	1.15%
Growth	*-3.04%*	*-5.73%*	*4.62%*	*-1.82%*	*-10.16%*		*-3.22%*

Figures in millions expect per share data

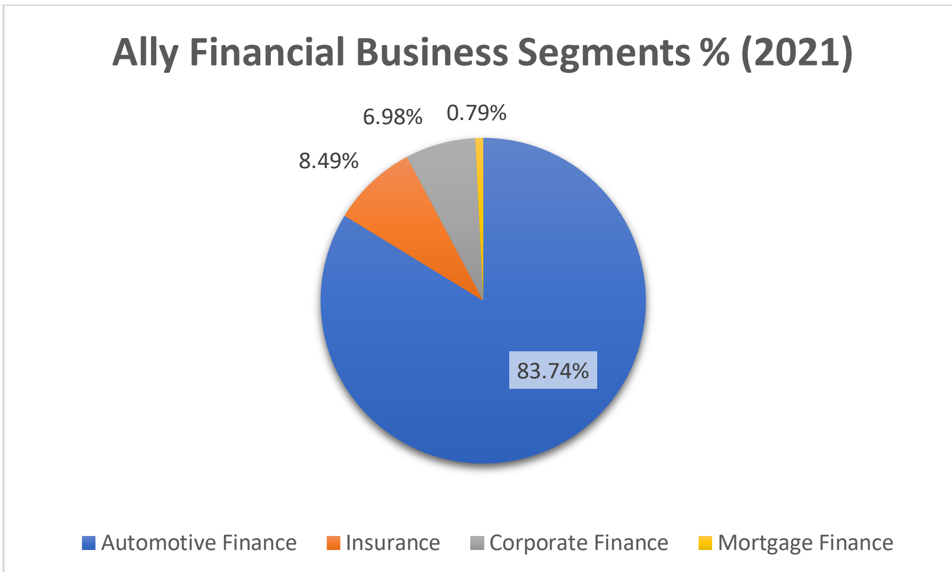
Table 2: Valuation Components

Ally Financial Inc (ALLY)	
Financial	*<=Industry*
Regional Banks	*<=Sub-Sector*
Current Price:	$29.29
Shares Outstanding:	313
Market Cap	**$9,171**
+ Long-term Debt (BV)	16,984
- Cash & Due from Banks	502
Enterprise Value	**$25,653**
Beta	1.92
P/E (next 12 months)	4.08
52-week low	$28.00
52-week high	$56.28
Dividend Yield (current)	0.02%
Dividend Yield (per FactSet)	4.30%

ECONOMIC EFFECTS OVERVIEW

The Fed continued to hike Fed Funds rate another 75bps during the last FOMC meeting on September 21, 2022, which now ranges from 3% to 3.25%. The Fed maintains aggressive stance with the hope of beat down inflation expectations and stabilizing rapidly rising prices. Market consensus believe there is a higher probability of another 75bps hike for the meeting in November 2022 (**Exhibit C**). Higher rates translated to higher borrowing costs which may decrease profitability for firms. The average retail prices of new cars sold in 2022 have gone up 11.5%, and used cars prices have gone up 40.5% from a year ago due to supply constraints. Ally Financials benefited from near zero-interest rates combined with low supply in early 2021. The company experienced explosive growth in net financing revenue, driven by lower deposit costs, higher gains on off-lease vehicles, and higher retail auto revenue. However, the rising rate combined with the high inflation economic environment in

2022 may present some challenging headwinds to the auto vehicle segment, dampening growth and earnings potential of loan companies like Ally Financials. In October, the largest US banks issued a warning of dangers that lurks ahead in auto loans as used cars prices slumps 7% in the third quarter leaving borrowers with a dilemma that affect the decision of whether they should continue making payments. Consumers may avoid or delay on purchasing and financing big-ticket purchases until more favorable rates present themselves in the future. The possibility of an economic slow-down may pose greater risks on Ally Financials due to its high concentration of auto loan composition.



FINANCIAL COMPARISON

PROFITABILITY

2. PROFITABILITY Factors (1 - best, 6 - worst: high is better)									RANK							
Company Name	EPS 3Y Growth	NIM	EBIT Margin (NTM)	ROA	ROE	ROIC	Beta *(3 Yr.)*	Sales	EPS 3Y Growth	NIM	EBIT Margin (NTM)	ROA	ROE	ROIC	Avg. Rank	*Evaluation*
Ally Financial	**75.27%**	**3.95%**	**43.1%**	**1.4%**	**15.9%**	**9.1%**	**1.92**	**10,729**	**2**	**2**	**6**	**4**	**3**	**4**	3.5	*Profitable*
Valley National	4.22%	3.43%	52.2%	0.9%	8.2%	6.0%	1.14	1,497	5	3	3	5	6	6	4.7	*Less Profitable*
Discover Financial Services	78.82%	10.94%	61.4%	4.0%	33.3%	15.7%	2.07	12,798	1	1	2	2	1	1	1.3	*More Profitable*
BankUnited	39.34%	2.26%	49.1%	0.9%	12.0%	9.4%	1.32	1,096	4	5	5	6	4	3	4.5	*Less Profitable*
First Horizon	-18.90%	2.74%	51.2%	95.7%	10.0%	8.3%	1.28	3,238	6	4	4	1	5	5	4.2	*Less Profitable*
Synchrony Finl	42.76%	-	64.7%	3.9%	26.7%	14.6%	1.80	11,224	3		1	3	2	2	2.2	*More Profitable*
Average	*0.37*	*0.05*	*0.54*	*0.18*	*0.18*	*0.11*	*1.59*									

- **3-Year EPS Growth:** Ally Financial (75.27%) shows a significant outperformance over almost all its peers, came second to Discover Financial Services (78.82%). The meteoric rise in Ally Financial revenue in 2021 was due to the supply shortage of automobiles combined with the price increase of new and used vehicles. The company's revenue benefited from higher outstanding loan balances of the price increase. While the company experienced a surge in revenue growth in the past year, 2022 presented more challenging environment which hindered and dampened its growth performance. Ally Financial's pre-tax income from continuing operations for Q2 2022 declined $408 million from Q2 2021 (as presented in **Exhibit A)**.

- **Net Interest Margin (NIM)**: Ally Financial (3.95%) ranked 2nd amongst its peers with a decent NIM, showing that it is still relatively profitable from its interest revenue. However, since interest rates in the economy significantly affect the NIM, this may indicate trouble for Ally Financial. The Fed fund futures market sentiment for November 2022 showed a 46.8% expected rate increase to 350-375 bps and 53.2% to 375-400 bps (as shown in **Exhibit B)**. The market consensus appears to maintain a certain degree of conviction that interest rates are likely to continue to rise in the future. Consumers are more likely to borrow money when interest rates are low, resulting in higher NIM. On the contrary, loans become less attractive when interest rates rise, causing NIM to decline
- **EBIT Margin (NTM):** Ally Financial margin ratio of 43.0% from Q4 2021 ranked worst out of its peers and has since declined to 29.20% in Q2 2022. The deterioration in EBIT margin could indicate lower profitability from the company.
- **Return On Invested Capital (ROIC):** Ally Financial (9.1%) appears to fall in the bottom tier compared to its peers, which may indicate that the company may be less effective in generating returns on its investment.

LEVERAGE

3. LIQUIDITY, CASH FLOW, DEBT (1 - best, 6 - worst: high is better for current ratio and EBITDA/Int. Exp; low is better for Debt/EBITDA and Beta)

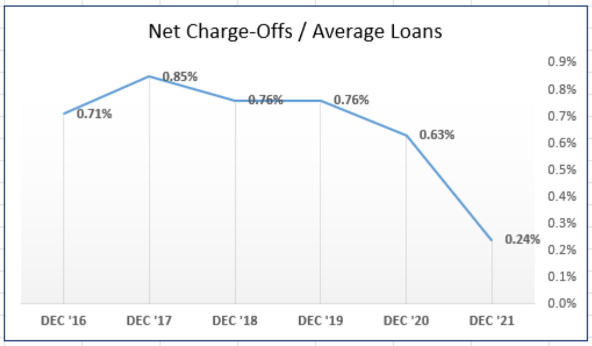
								RANK							
Company Name	[1]Tier 1 Ratio	[2]NCO Ratio	[3]NPLs / Loans	Dividend Yield	FCF Yield	Total Debt/EV	Diluted Shares	Tier 1 Ratio	NCO Ratio	NPLs / Loans	Dividend Yield	FCF Yield	Total Debt/EV	Avg. Rank	*Evaluation*
Ally Financial	11.1%	0.2%	1.1%	1.85%	-5.35%	71.4%	324.0	4	3	5	5	6	5	4.7	*More Risk*
Valley National	9.5%	0.0%	0.7%	3.20%	11.68%	38.3%	508.5	5	1	3	2	4	2	2.8	*Avg. Risk*
Discover Financial Services	15.2%	1.7%	0.89%	1.63%	16.80%	56.7%	279.0	1	5	4	6	3	3	3.7	*Avg. Risk*
BankUnited	11.3%	0.3%	0.6%	2.17%	9.09%	63.3%	79.4	3	4	2	3	5	4	3.5	*Avg. Risk*
First Horizon	11.6%	0.0%	0.5%	3.67%	32.00%	22.2%	569.4	2	1	1	1	1	1	1.2	*Less Risk*
Synchrony Finl	-	2.9%	-	1.90%	26.88%	73.3%	495.3		6		4	2	6	4.5	*More Risk*
Average	*0.12*	*0.01*	*0.01*	*0.02*	*0.15*	*0.54*									

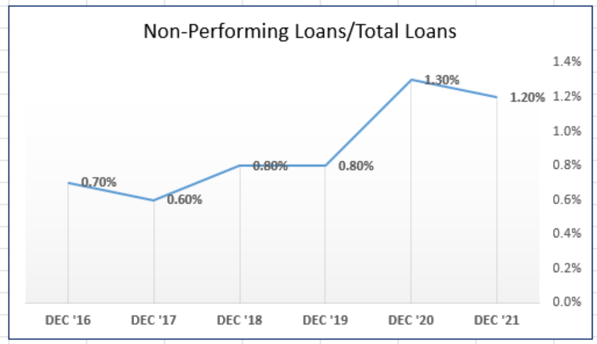
[1] Equity capital and reserves vs. risk-weighted assets *[2] Percent of loans 'written off' as non-collectible* *[3] Percent of loans not making payments*

- **Free Cash Flow (FCF) Yields & Total Debt/EV:** Ally Financial received the worst ranking in FCF Yield (-5.35%) with the second worst ranking in having the highest Total Debt/EV ratio (71.4%). The company can be perceived as a risky investment since it is highly levered and may have insufficient cash flow to fulfill its future obligations.
- **Tier 1 Ratio (T1R):** Ally Financial (11.1%) is slightly lower than First Horizon (11.6%) and Bank United (11.3%). According to Bassel III, the minimum risk-weighted assets in T1R capital required is 6%, and Ally Financial exceeds that by 5.1%. Discover Financial appears to outperform Ally Financial by 4.1% in this ranking. However, Ally Financial may risk its T1R deteriorating if the economy continues to slow. While Ally Financial's T1R showed that it is may be able to absorb mild to moderate unexpected loss and continue operation as a going concern, its negative FCF yields of -5.35% shows that the company might not have sufficient cash flow to satisfy its obligations.
- Ally Financials' **Net Charge Off (NCO) Ratio** of 0.2% ranked 2nd in having the least amount of loans that are 'written-off' as non-collectible. Valley National and First Horizon came in 1st place with 0% of NCO. Ally Financial loans composition has a higher concentration in consumer and installment lending than Valley National and First Horizon. Since a substantial portion of Ally Financial's business is in auto financing, this may explain why the NCO is slightly higher than its Regional Bank peers. Ally Financial's

NCO ratio is likely to surge in a rising rate and inflationary environment since its concentration in auto loans carries more risk.

- Ally Financials' **Non-Performing Loans (NPL) Ratio** of 1.1% is slightly higher than Discover Financial of 0.9%. The current NPL ratio indicates that the level of the borrowers making payments is higher than defaulting on the loans. However, Ally Financial is likely to face the risk of a rise in NPL ratio as real wages are impacted by inflation, consumer spending decline, and a slow-down in the automobile segment.





Overall, Ally Financials appear to carry more risks compared to its peer due to its high concentration in consumer installment in auto financing. The uncertainty in the environment may present unfavorable headwinds for Ally Financials.

VALUATION ANALYSIS

PEER COMPARISON

5. BOND COMPARISON

Company Name	Cusip	Coupon	Maturity	Credit Rating (Moodys/S&P)	YTW	OAS (Trsy)	Altman Z-score (Bloomberg)	Price	Duration	Yield Spread	Default Risk	Int. Rate Risk	Financial Risk	Weighted Rank
									Adjust weight if desired by changing these figures=>	*2.0*	*3.0*	*3.0*	*3.0*	
Ally Financial	370425RZ5	**8.000%**	**11/2031**	**Baa3/BBB-**	**7.15%**	**337**	**0.19**	**$104.53**	**6.25 yrs.**	**2**	**1**	**3**	**5**	**2.7**
max 2 bonds per company														
Valley National	191794AE7	3.000%	6/2031	Baa3/BBB-	5.91%	225	0.28	$88.58	7.27 yrs.	5	2	5	3	**3.6**
Discover Financial Services	25472CBJ7	4.000%	11/2031	Baa3/BBB-	5.94%	225	1.15	$85.94	7.24 yrs.	6	5	4	4	**4.5**
BankUnited	06652KAB9	5.125%	6/2030	Baa2/BBB-	6.09%	238	0.38	$94.49	6.10 yrs.	3	4	2	4	**3.1**
First Horizon	337158AJ8	5.750%	5/2030	Baa3/BBB-	6.02%	229	0.28	$98.22	5.89 yrs.	4	2	1	1	**1.9**
Synchrony Finl	87165BAR4	2.875%	10/2031	Baa3/BBB-	7.12%	345	1.15	$91.62	7.40 yrs.	1	5	6	5	**4.4**
					Average OAS and Z-score:	*26651.40%*	*57.17%*							

Overall Ranking: 2nd

Ally Financial ranked 2nd in the weighted quantitative measures compared to its peers with similar credit ratings and duration. Ally Financial has the 2nd highest yield spread yet also carries the highest default risk and financial risk than its peers. Ally Financial split rating of Baa3/BBB- the risk of its rating falling below investment grade could cause the bond price to drop substantially. The TCM Bond team believes it is an appropriate time to de-risk our bond portfolio to shift to a better opportunity in the high inflation and rising rates environment. The portfolio already has a significant sector allocation to IG Corp and a substantial portion below-investment grade. Therefore, Ally Financial is deemed unfavorable to our current portfolio, given the likelihood of a slowing economic condition.

Option-Adjusted Spread (Treasury): 2nd

Ally Financial ranked the 2nd in having the highest yield spread compared to its peers, posing more credit risk in the current economic environment. While, the bond offers a higher YTW of 7.15%, it may be perceived as a riskier bet rather than an attractive investment compared to its peers. If the bond is perceived as a riskier asset, investors may react by selling their holdings and as a result, the price of the bond declines.

Default Risk: 1st

Ally Financial ranked 1st in having the lowest Altman Z-score (0.19), indicating that it has the highest default risk out of its peers. The company does have a healthy Tier 1 Ratio that showed it has the capacity to absorb unexpected loss in times of financial distress.

Interest Rate Risk: 3rd

Even though Ally Financial ranked 3rd amongst its peers, it carries a longer duration of 6.27 years that may react more sensitively to the fluctuation of interest rates. The TCM Bond team believes that rates are likely to continue to rise for the remainder of the year which may result in the decline in price of the bond.

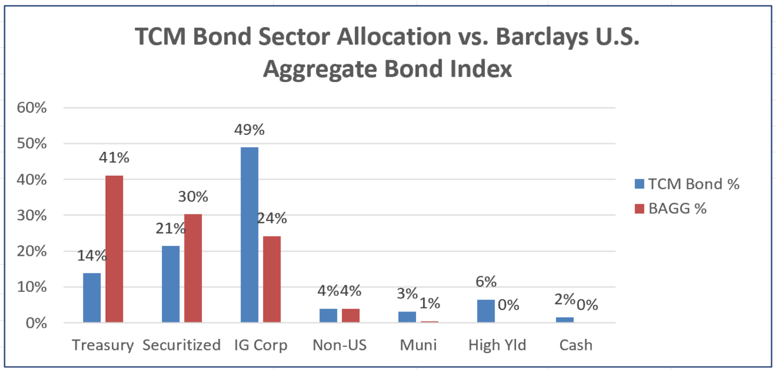
Financial Risk: 5th

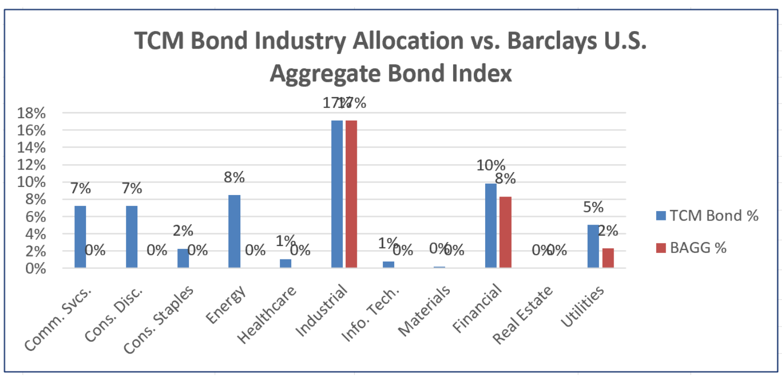
Ally Financial ranked 5th amongst its peers in having the highest financial risk with a Total Debt/EV ratio of 71.4% combined with a negative FCF yield of -5.35%.

PORTFOLIO IMPACT AND SUMMARY

The TCM Bond team recommends a sell of Ally Financial Inc. 8.00% 2031 bond [370425RZ5] to allocate the proceeds to higher credit quality securities with similar duration. The sell on this bond aligns with our team strategy to exit lower credit quality bond since Ally Financial bond is rated BBB- (S&P) and offers a yield-to-worst of 7.15% (324.55 bps OAS). Our team plan to replace the bond with another asset with duration that aligns with our strategy to bring the portfolio duration closer to the Bloomberg Aggregate Index.

The current TCM bond portfolio shows an overweight in the IG Corp sector and a significantly underweight in Treasury. The sell of Ally Financial will reduce the exposure to IG Corp sector, raising funds to potentially allocate to the Treasury sector. The current allocation of the TCM bond industry have 10% exposure which will get reduced if Ally Financial gets sold off.





APPENDIX

EXHIBIT A

Ally Financial Report Second Quarter 2022

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Pre-Tax Income by Segment

($ millions)	2Q 22	1Q 22	2Q 21	Increase/(Decrease) vs. 1Q 22	Increase/(Decrease) vs. 2Q 21
Automotive Finance	$ 600	$ 725	$ 917	$ (125)	$ (317)
Insurance	(122)	13	87	(135)	(209)
Dealer Financial Services	**$ 478**	**$ 738**	**$ 1,004**	**$ (260)**	**$ (526)**
Corporate Finance	60	64	95	(4)	(35)
Mortgage Finance	6	11	—	(5)	6
Corporate and Other	90	33	(57)	57	147
Pre-Tax Income from Continuing Operations	**$ 634**	**$ 846**	**$ 1,042**	**$ (212)**	**$ (408)**
Core OID[1]	10	10	9	—	1
Change in Fair Value of Equity Securities[2]	136	66	(19)	71	156
Repositioning and Other[3]	—	—	70	—	(70)
Core Pre-Tax Income[4]	**$ 780**	**$ 921**	**$ 1,102**	**$ (141)**	**$ (321)**

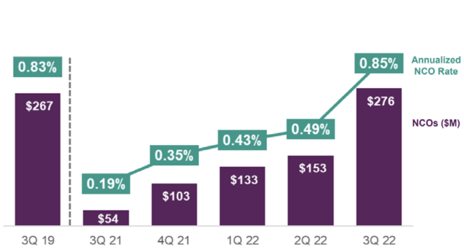
(1) Core OID for all periods shown is applied to the pre-tax income of the Corporate and Other segment. Refer to the Definitions of Non-GAAP Financial Measures and Other Key Terms and Reconciliation to GAAP later in this release.
(2) Change in fair value of equity securities impacts the Insurance and Corporate Finance segments. Reflects equity fair value adjustments related to ASU 2016-01 which requires change in the fair value of equity securities to be recognized in current period net income as compared to periods prior to 1/1/2018 in which such adjustments were recognized through other comprehensive income, a component of equity.
(3) Repositioning, net of tax in 2Q 2021 includes a $70 million charge related to loss on extinguishment of debt associated with the redemption of TRUPs
(4) Core pre-tax income is a non-GAAP financial measure that adjusts pre-tax income from continuing operations for Core OID, equity fair value adjustments related to ASU 2016-01, and repositioning and other primarily related to the loss on extinguishment of debt associated with the redemption of TRUPs. Management believes core pre-tax income can help the reader better understand the operating performance of the core businesses and their ability to generate earnings. Refer to the Definitions of Non-GAAP Financial Measures and Other Key Terms later in this release.

SOURCE: ALLY FINANCIALS PRESS RELEASE

EXHIBIT B

Ally Financial Report Third Quarter 2022

Consolidated Net Charge-Offs (NCOs)



Note: Ratios exclude loans measured at fair value and loans held-for-sale. See page 31 for definition.

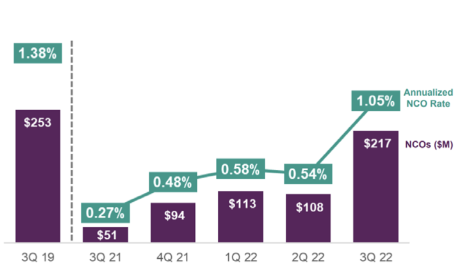
Net Charge-Off Activity

($ millions)

	3Q 19	3Q 21	4Q 21	1Q 22	2Q 22	3Q 22
Retail Auto	$ 253	$ 51	$ 94	$ 113	$ 108	$ 217
Commercial Auto	1	-	-	(1)	(1)	-
Mortgage Finance	-	-	-	-	(1)	1
Corporate Finance	15	-	1	-	26	31
Ally Lending	-	5	9	15	13	16
Ally Credit Card (1)	-	-	2	8	11	13
Corp/Other(2)	(2)	(2)	(3)	(2)	(3)	(2)
Total	**$ 267**	**$ 54**	**$ 103**	**$ 133**	**$ 153**	**$ 276**

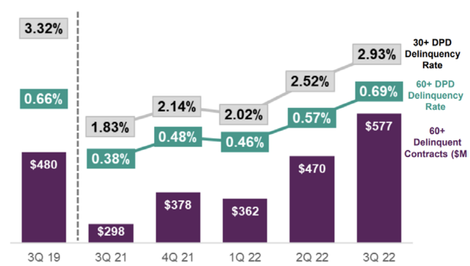
(1) 4Q'21 Ally Credit Card NCOs represent December 2021 activity only
(2) Corp/Other includes legacy Mortgage HFI portfolio.

Retail Auto Net Charge-Offs (NCOs)



See page 31 for definition.

Retail Auto Delinquencies



Note: Includes accruing contracts only. Days Past Due ("DPD")

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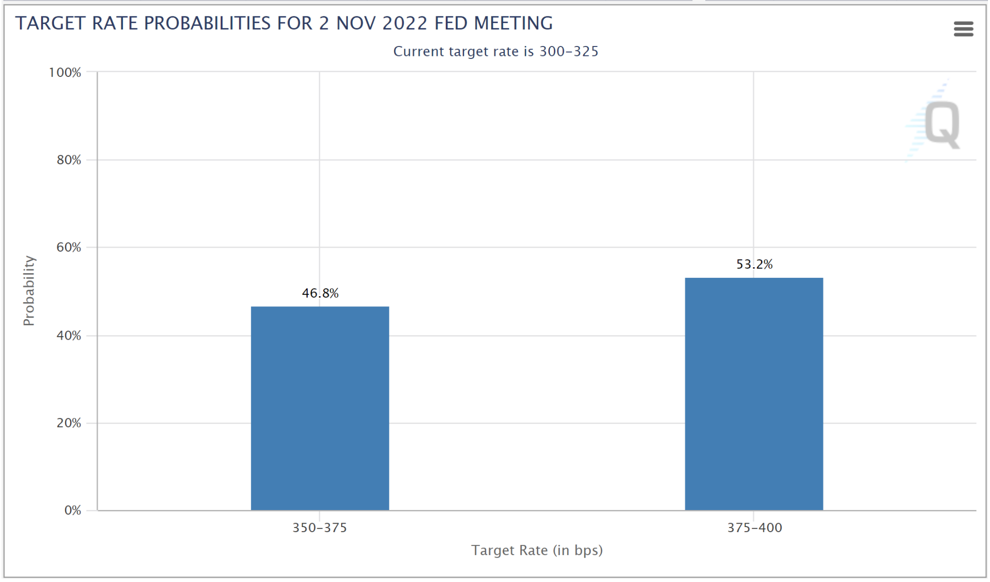
SOURCE: ALLY FINANCIALS PRESS RELEASE

EXHIBIT C

Market Consensus as of October 1, 2022

MEETING INFORMATION						PROBABILITIES		
MEETING DATE	CONTRACT	EXPIRES	MID PRICE	PRIOR VOLUME	PRIOR OI	EASE	NO CHANGE	HIKE
2 Nov 2022	ZQX2	30 Nov 2022	96.3000	57,852	350,961	0.0 %	0.0 %	100.0 %



Market Consensus as of October 22, 2022

SOURCE: CME GROUP

REFERENCES

FactSet

Ally Financial Reports Second Quarter 2022 Financial Results:
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