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Recommendation: SELL
The Company

Founded in 1982 as MNC Financial, MBNA Corporation is currently a holding company with three primary banks, MBNA America Bank, MBNA Europe Bank Limited, and MBNA Canada Bank. It is the largest independent credit card lender in the world and also offers deposit and insurance services, consumer loans, and business credit cards. The company primarily markets through professional, educational, recreational, and charitable organizations, recruiting clients through NASCAR, the Marine CORPS and The National Hockey League as well as through agreements with around 300 financial institutions. Affinity card marketing has been a major contributor to bottom-line in recent years. It has also consolidated through the acquisition of companies such as PNC Financial Services, SunTrust Banks, First Union, Comercia, AmSouth Bancorporation, Abbey National, and Premium Credit Ltd.

MBNA has announced that it will start issuing its own American Express cards later this year and is currently under pressure from shareholders to create a more independent board of directors.

BASIC INFORMATION	
Sector	Finance
Industry	FINANCIAL SERVICES
Current Price	\$24.44
Market Cap.	\$31.23 billion
Average Volume	5470830
52 Week Low	\$22.35
52 Week High	\$29.68
Annual Dividends	\$0.56
Yield	2.29%
Trailing P/E (last 4-qtr)	11.86
Forward P/E (next 4-qtr)	10.86
Beta	1.28627
Shares Outstanding	1277.67 million

The Industry

- Steady Consolidation: Banking.
- Shift From Private To Public.
- Above average growth plus improved profit margins.
- Risk Management has improved over last decade.
- Expect M&A to continue but be less of a positive.
- Expect banks to under perform: Industry is not so bullish, increased competition, flatter yield curve, and perception of more earnings upside in other sector.

Some recent industry earnings growth have been supported by items that aren't sustainable, raising earnings quality concerns.

The Bank Industry's Timeliness rank continues to hover in the bottom quartile of the Value Line Universe.

Banks are having an increasingly difficult time achieving growth in revenues: net interest income and fees from recurring activities, like lending, deposit taking, and providing investment and processing services

Investment Analysis Highlights:

- Large Caps will out perform mid-caps.
- The company's forecast is limited by the limited growth potential.
- MBNA has shown no movement during its time in the portfolio.
- Companies most likely to outperform are those with competitive advantages, defined revenue streams, and records of consistent earnings growth. MBNA does not fit this profile.



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Investment Analysis Discussion

Steady Consolidation: Banking, thrift and capital markets businesses have been merging over the past two decades leading to an increase in larger companies.

- **Shift From Private To Public:** Commercial real estate ownership, thrifts, and insurance companies, have shifted from private to public ownership.
- **Above average growth plus improved profit margins:** Financial services on average grow faster than nominal GDP.
- **Risk Management has improved over last decade:** Better management, increased regulation, and risk shifting tools like derivatives and securitization.
- Standard & Poor's is currently projecting real GDP growth of 3.7% in 2005.
- **Expect M&A to continue but be less of a positive:** expect fewer high premium deals since valuations are already high and most key franchise are out of the market.
- **Expect banks to under perform: Industry is not so bullish,** increased competition, flatter yield curve, and perception of more earnings upside in other sector.
- **Large Caps will out perform mid-caps:** Large-caps are trading around 15% below historical relative levels to mid-caps. There is more upside earning in large caps (magnified if stock market does better than expected). M&A will cause an even smaller boost on small-cap.
- **Companies most likely to outperform are those with competitive advantages, diversified revenue streams, and records of consistent earnings growth.**
- When the economy is strong, businesses want to borrow to fund expansion. Similarly, when job markets are favorable and consumer confidence is up, demand for consumer credit increases. Standard & Poor's is currently projecting real GDP growth of 4.8% in 2004 and 3.7% in

2005. Such changes in environment would be favorable for banks with a commercial focus — particularly large-capitalization banks, which in aggregate appear to have put many regulatory, corporate governance, and credit-quality issues behind them.

- As interest rates rise and the yield curve flattens, there core deposit growth should slow as will stock performance.
- In the last several quarters, mortgage volume has slipped from its recent record-high levels, and we expect it to continue to fall. However, we believe that home equity lines will offset some of the drop in mortgage refinancing.
- Fluctuations in interest rates, while important, do not have an absolute influence over the net interest margins of commercial banks, primarily because banks are able to adjust to such fluctuations. In theory, banks can match the maturities of their assets (loans and investments) and liabilities (deposits and borrowings) so that rates earned and rates paid move more or less in tandem, while net interest margins remain relatively stable. In practice, however, banks can — and do — deviate from a perfectly balanced position.
- MBNA also faces risk from a weaker than expected economy (3%-3.5% over the next twelve months) which would cause increased credit costs, beyond expectations (especially if consumers weaken).
- MBNA has faced constant pressure to make its management team more independent. This seems to be a constant theme that will not easily be resolved within the company and will hinder its progress.

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Comparable Analysis:

continue to perform passively as it has done during its time in the portfolio.

- Although MBNA is trading cheap relative to its industry peers, we believe that it has limited growth potential and that the stock will

Company Name	Footnote	Comp Aggregate	Citigroup C	MBNA KRB	Wells Fargo WFC	Synovus Financial SNV	Bank of America BAC
<i>(LFY Income Statement):</i>							
Latest Fiscal Year End Date	1	31/12/03	31/12/03	12/31/03	31/12/03	31/12/03	31/12/03
Revenue	2	\$189,634,185,000.0	\$94,713,000,000	\$11,684,364,000	\$31,800,000,000	\$ 2,430,821,000.00	\$49,006,000,000
Gross Profit	3			\$10,576,558,000	\$30,187,000,000	\$ 2,213,260,000.00	\$44,098,000,000
EBITDA	4	\$88,521,207,000.0	\$45,725,000,000	\$4,145,855,000	\$15,580,000,000	\$ 831,352,000.00	\$22,239,000,000
<i>(Per Share Income Statement Data)</i>							
LTM EPS Date	5		10/12/04	10/12/04	10/12/04	10/25/04	10/12/04
LTM EPS*	6		\$3.04	\$1.95	\$3.90	\$1.34	\$3.72
CFY EPS Estimate	7		\$4.02	\$2.05	\$4.18	\$1.45	\$3.67
NFY EPS Estimate	8		\$4.41	\$2.32	\$4.65	\$1.65	\$4.03
*Excl. extra. Items, writeoffs, & one time charges							
<i>(Balance Sheet Data - Most Recent Quarter):</i>							
Cash and Cash Equivalents	9	\$412,410,145,000.0	\$276,245,000,000	\$5,462,690,000	\$26,310,000,000	\$710,455,000	\$103,682,000,000
Total Debt (incl. ST Debt and leases)	10	\$737,504,830,000.0	\$402,487,000,000	\$23,658,048,000	\$88,166,000,000	\$2,800,782,000	\$220,393,000,000
Total Common Equity (Book Value)	11	\$190,535,833,000.0	\$98,014,000,000	\$10,352,027,000	\$32,014,000,000	\$2,175,806,000	\$47,980,000,000
<i>(Stock Data):</i> Stock Price As Of:							
Stock Price	12		10/12/04	10/12/04	10/12/04	10/25/04	10/12/04
Common Shares Outstanding	13		\$44.80	\$24.92	\$60.46	\$27.00	\$45.53
Market Capitalization (MV of Equity)	14	\$577,883,166,740.0	5,180,260,000	12777000.0	1,690,340,000	314,638,000	5,156,950,000
Total Mkt. Capitalization (Tot. Net Debt+MV of Equity)	15	\$902,977,851,740.0	\$232,075,648,000.0	\$318,402,840.0	\$102,197,956,400	\$8,495,226,000	\$234,795,933,500
<i>(Financial Ratios excl. debt ratios-see Risk Section)</i>							
LFY Gross Margin	16		NA	90.5%	94.93%	91.05%	89.98%
LFY EBITDA Margin	17		48.3%	35.5%	49.0%	34.2%	45.4%
ROE	18	24.8%	16.0%	0.2%	20.55%	19.42%	40.00%
ROA	19	9.5%	9.1%	12.2%	13.0%	16.7%	8.3%
Receivable Turnover	20		NA	N/A	NA	NA	NA
Inventory Turnover	21		NA	N/A	NA	NA	NA
Current Ratio	22		0.66	0.383090306	0.06	0.05	0.32
<i>(Growth/Return):</i>							
Historical 3 Year Revenue Growth Rate	23		1.8%	12.0%	7.6	5.8	6.5
Historical 3 Year EPS Growth Rate	24		16.9%	32.0%	14.1	6.5	16.9
Projected ROE (NFY)	25		23.31%	0.29%	24.55%	23.86%	43.31%
CFY - NFY EPS Growth Rate	26	10.0%	9.70%	0.131707317	11.24%	13.79%	9.81%
Proj. Growth in EPS 5 Years	27	18.4%	21.1%	13.0%	12.00%	15.00%	18.00%
Dividend Yield	28		3.6%	1.9%	3.18%	0.69%	4.15%
VL Timeliness	29		2	3	3	3	
<i>(Risk):</i>							
Beta	30	1.01	1.36	1.6	1	1.1	0.67
VL Safety	31		3	3	3	2	
LT Debt / Market Capitalization (MV of Equity)	32	1.28	173.43%	7430.2%	86.27%	32.97%	93.87%
LT Debt / Common Equity (BV of Equity)	33	0.21	410.64%	228.5%	275.40%	128.72%	459.34%
<i>(Valuation):</i>							
MV of Equity / Book Value	34	3.03	2.4	1.8	3.2	3.9	4.9
LTM Price / EPS Ratio ("P/E")	35	13.77	14.8	12.8	15.5	20.1	12.2
CFY Price / EPS Ratio ("P/E")	36	12.22	11.1	12.2	14.5	18.6	12.4
NFY Price / EPS Ratio ("P/E")	37	11.11	10.2	10.7	13.0	16.4	11.3
Total Market Capitalization / EBITDA	38	10.20	7.84	4.5	10.53	12.73	15.81
Relative P/E (CFY)	39		0.7	0.68			
CFY P/E to CFY-NFY EPS Growth Rate	40	1.22	1.15	0.92	1.29	1.35	1.26
CFY P/E to Proj. Growth in EPS 5 Years	41	0.66	0.5	0.94	1.2	1.2	0.7
EV	42	490567706740.00	82072648000.00	13051070840.00	137743956400.00	9875098000.00	247824933500.00
EBIT	43	\$4,529.2	3966.00	563.00	6.45%	4.97%	8.17%
ev/ebit	44	108312316.17	20694061.52	23181298.12	2135932188751.99	198531381980.64	3031560779756.85
ev/ebitda	45	5.54	1.79	3.15	8.84	11.88	11.14

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DISCOUNTED CASH FLOW ANALYSIS:

The discounted cash flow analysis was centered on the Flow to Equity model and revealed an intrinsic value of \$ 79.93 per share. This supports the Hold recommendation, as the stock is currently undervalued at \$62.46 and has been very stable in its price.

Why only the Flow to Equity Model:

The reasoning goes back to the differentiation of debt for banks. Liabilities or so - called "debts" of a bank are really money owed back to their depositors - these debts are "operating expenditures" - but if they were used in the other valuation methods they would be treated as "financing expenditures"...meaning they would be treated like "debt" even though in the case of a bank they are NOT debt in the traditional sense. EFCF pulls in the changes in ALL the balance sheet items and does not separate the debt out - therefore it affords the analyst the ability to treat the "debt" (which is really the deposits) more like an operating line item than a financing line item (really money owed back to their depositors - these debts back to their depositors are "operating expenditures". The EFCF models Net Interest Income.

\$24.40

Risk Free Rate:	3.60%
Equity Market Risk Premium:	7.00%
Long term inflation:	2.50%
Terminal Growth:	5.00%
Equity beta based on Bloomberg:	1.3
No. of shares (diluted):	310
Current Market Price per share:	\$24.44

ASSUMPTIONS:

Net PPE: Historical Net PPE was fairly stable, showing minimum growth. So expected capital expenditure and depreciation growth were kept at the same rate in order to maintain net PPE stable.

Growth Sensitivity Analysis:

<i>Total Equity Value Per Share (a):</i>		4.00%	4.50%	5.00%	5.50%	6.00%
Terminal Growth in EFCF						
R(e)						
14.70%		\$17.8	\$18.4	\$19.0	\$19.6	\$20.4
13.70%		\$19.7	\$20.5	\$21.3	\$22.2	\$23.2
12.70%		\$22.3	\$23.3	\$24.4	\$25.7	\$27.2
11.70%		\$25.7	\$27.1	\$28.7	\$30.6	\$32.8
10.70%		\$30.3	\$32.4	\$34.8	\$37.7	\$41.2