SPECTRUM
Asset Management

2020 US Bank Results
So Far, So Good

29 July 2020

What Happened?

The US banks have performed relatively well, considering the profound stresses the COVID-19 pandemic is having on the economy. This is a testament to their stronger capital and reduced risk appetites post-Global Financial Crisis (GFC), as well as their good core earnings. For US banks, the COVID-19 pandemic appears to be an income statement, rather than a balance sheet problem like in the GFC — a big difference. In addition, **policymakers view banks as part of the solution, with banks being key conduits for government-driven stimulus.**

In 2Q20, more than 75% of the top 20 banks posted positive earnings, though net interest margins (NIM) were squeezed, reflecting Fed monetary easing and higher deposit levels driven by customers' precautionary liquidity and unspent stimulus money. However, Fed-driven easing also boosted mortgage banking revenues. This NIM squeeze could continue into 3Q20, with easing expected in 4Q20. Banks with capital markets operations had strong to very strong results from trading and underwriting. Loss reserves were also strengthened, with the top 20 banks more than doubling reserves since YE19**. We are encouraged that US regulators continue to allow healthy banks to pay dividends.**

What's Next?

There are still numerous stresses on US banks' revenues and loss provisions.

- COVID-19 infection and cure rates remain unknown, and the world is still learning about how this disease works. While massive global resources are being devoted to developing a vaccine, the timing and effectiveness are uncertain. Thus, a 'second wave' is possible, and if it is severe enough, more lockdowns could occur. And if widespread, economic dislocation could be substantial, with higher levels of borrower distress.
- The federal and state governments have extended historic levels of monetary and fiscal support to those affected by the pandemic. This support has been a big plus for banks' loan quality. But, how long will such support continue, and in what form?
- Loan deferrals and moratoria could result in write-offs later in 2020 and in 2021 by banks, depending on the shape and strength of the recovery, and government stimulus.
- The rapid shift to more digital banking will be a key, enduring result of the pandemic — positive for banks and investors who have been waiting to enjoy the low-cost efficiency of digital investments. This would help to boost bank earnings.

Despite an uncertain path to recovery, Spectrum is encouraged by strong US bank fundamentals going into this pandemic, and by the banks' ability to post earnings while increasing reserves. With caution, we believe US banks are well positioned to meet the economic stress of COVID-19.

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