Investment News: Money Morning

Investment News Provider

- Home
- Archives
- Premium Content
- Investor Reports
- About Us
- Contributors
- Contact Us
- Categories

Wednesday, February 18th, 2009

The Top 12 U.S. Banks: From Zombies to Hidden Gems

By Martin Hutchinson
Contributing Editor
Money Morning

U.S. Treasury Secretary Timothy Geithner last week proposed a series of programs, totaling $1.5 trillion, to bail out the U.S. banking system. Of course, Geithner hasn't told us precisely how he plans to spend the money, or identified which banks require such an enormous outlay.

So I thought it was worth looking at the United States' 12 largest banks to see where the problems might be and identify which banks might need big infusions of government cash. I perused the financial statements of all 12 banks, and also looked at their market valuations.

Unlike when the Troubled Assets Relief Program (TARP) was proposed in September - when the projections for potential losses were largely financial conjecture - we now have important concrete data on the banking system's troubles; namely, each of the bank's annual financial reports for 2008.

Those figures were calculated with the most current knowledge of the economy's housing crisis and other related financial disasters, and with the potential for losses on "bad assets" fully taken into account and examined in detail by auditors. Further economic bad news might weaken new batches of assets, but at least the biggest problems should by now be fully apparent.

There is a lot of information - both about potential bailout needs and possible investment bargains - which we can gain from the banks' annual earnings figures. For instance:

- Banks that made profits in the very difficult fourth quarter of 2008 are probably in good shape, especially if their loan-loss provisions exceeded their charge-offs (the amount actually lost).
- Even banks that lost money in the fourth quarter - an exceptionally harsh three months - have no immediate need for funding, provided they made money the rest of 2008 and seem likely to resume making money going forward.
- In this context, management's dividend policy is a good indicator: If the dividend is maintained, rather than being sharply cut or suspended, management is probably genuinely confident about the bank's position and outlook.
- Another good indicator of a bank's health - at least of the market's perception - is the ratio of share price to book value. If that's below 25% or so the market lacks confidence in the bank's ability to solve its problems.

Using these indicators, we can assess the viability of the leading U.S. banks. Each bank can then be classified with one of our four "official" ***Money Morning*** designations. These designations, or labels, consist of:

- **Zombies**: Institutions kept alive only by TARP funding. These subtract value from the economy and should be put out of their misery through controlled liquidation, with the healthy parts being salvaged.

- **Walking Wounded**: These banks may need a little bit more help, but are currently operating adequately on their own. One caveat: An intensification of economic downturn could push some of them into "zombie" status - or even bankruptcy.

- **Risky but Proud**: These banks have relatively high risks, because of acquisitions or their business models, but are operating at full blast and can hold their heads high for their success in dealing with 2008's enormous difficulties.

- **Hidden gems**: These banks have conquered 2008's difficulties, taken care of their bad debt problems, and still managed to make a substantial profit. Short of a repeat of what U.S. banks had to deal with from 1929-1933, as part of the Great Depression, these financial institutions should continue to operate in the black.

The Envelopes Please …

We listed the 12 largest U.S. banks by assets, as of Dec. 31, ignoring foreign-owned banks, Goldman Sachs Group Inc. (GS) and Morgan Stanley (MS) (those last two are onetime investment banks that are technically now commercial banks, but still possess a very different business mix. We give you a rundown on the financial stability of each one, and give each institution with the single-most-appropriate of our four official ***Money Morning*** designations. The Top 12 banks, biggest first, are as follows:

1. **Bank of America Corp. (BAC)** - ***Zombie***: BofA has about $2.8 trillion in assets including Merrill Lynch, which was acquired after the end of last year, and Countrywide Financial Corp., formerly the nation's No. 1 housing finance bank. It received $45 billion from TARP, plus $118 billion in guarantees against Merrill Lynch's assets. At Friday's closing share price of $5.17, the stock was

trading at 21% of book value (it closed at $4.90 yesterday). BofA posted a fourth-quarter net loss of $1.55 billion, plus a Merrill Lynch net loss of $15.3 billion, which forced BofA to cut its quarterly dividend to a nominal one cent per share. Judging by other banks' results, if Bank of America had made no acquisitions in 2008, it would be in solid shape. With the acquisitions, however, it's a basket case - and may well need even more federal funding.

2. **JPMorgan Chase & Co. (JPM)** - ***Risky but Proud***: JPMorgan has $2.175 trillion in assets, and received a $25 billion TARP investment. It's a major international bank with a large investment banking operation. It bought The Bear Stearns Cos. Inc., investment bank in March and the Washington Mutual Inc. thrift in September, both with Federal government help.

JPMorgan booked $702 million in net income in the fourth quarter and $5.6 billion in net income for all of 2008. The company also had a fourth quarter loan-loss provision of $8.5 billion and charge-offs of $4.5 billion. But there were also $2.9 billion worth of securities markdowns in the investment banking operation. Again, this bank is high-risk from an investment standpoint because of its acquisitions, but it appears to be in excellent shape with no immediate need for extra funding. Its Friday closing share price of $24.69 equates to 72% of net asset value, though it closed yesterday at $21.65, down 12.3%. It pays a quarterly dividend of 38 cents per share.

3. **Citigroup Inc. (C)** - ***Zombie***: Citi remains the nations' third-largest bank, with $1.9 trillion in assets. It received a $45 billion TARP investment, plus guarantees on $301 billion of assets. At Friday's close of $3.49, it was trading at 25% of book value. Citi lost $8.3 billion in the fourth quarter of 2008 and $18.7 billion for the whole year. It was finally forced to sell control over its Smith Barney brokerage operation to Morgan Stanley in January, and has reduced its dividend to a nominal penny a share. Citi has been a serial flirter with bankruptcy over the past 30 years and remains a basket case. There are a few good assets buried within the rubble - chiefly because the company is so large and diverse.

4. **Wells Fargo & Co. (WFC)** - ***Risky but Proud***: Wells Fargo has $1.3 trillion in assets, and garnered a $25 billion TARP investment. Originally a small bank based in San Francisco, Wells Fargo officially entered the heavyweight class with its acquisition of Wachovia Corp., late last year. Its Friday closing price of $15.76 equated to 104% of its book value, though it closed yesterday at $13.69. Wells Fargo's stock pays a quarterly dividend of 34 cents. The company posted a fourth-quarter net loss of $2.55 billion, not including an $11 billion net loss at Wachovia. Wells Fargo's full-year earnings totaled $2.84 billion. It had a fourth-quarter loan-loss provision of $8.4 billion, compared with actual charge-offs of $2.8 billion. Wachovia's 2006 acquisition of the California mortgage bank Golden West Financial puts Wells Fargo at risk, but the company's operations appear solid and it has no immediate need for extra funding.

5. **PNC Financial Services (PNC)** - ***Risky but Proud***: The Pittsburgh-based PNC has $291 billion in assets, after buying the slightly larger National City Corp in October. It also received a $7.6 billion TARP investment. At Friday's closing price of $28.20, PNC's shares were trading at 79% of book value. The company pays a quarterly dividend of 66 cents per common share, and posted a fourth-quarter net loss of $248 million (excluding costs associated with its acquisition of National City, the company had a fourth-quarter profit of $132 million}. PNC had provision for credit losses of $990 million, compared with net charge-offs of $207 million. This is one of the riskier banks because of the

difficulties in integrating National City and possible problems in National City's loan portfolio. But it appears to have no immediate need for funding and is currently profitable, and its stock is selling close to book value and paying a solid dividend. One final point: PNC's shares fell only 6.1% yesterday, a day when the shares of most major banks fell by more than twice than amount, perhaps hinting that investors perceive less risk in PNC's shares.

6. **U.S. Bancorp (USB)** - ***Hidden Gem***: U.S. Bancorp has $266 billion in assets, and received $6.6 billion in TARP funding. This regional banking firm is based in Minneapolis, and the company operates primarily in the upper Midwest and Northwest. With a closing price of $12.40 on Friday, USB shares were trading at 131% of book value (the shares closed yesterday at $10.73, down 13.47%). The company also pays a quarterly dividend of 42.5 cents per common share. U.S. Bancorp posted a fourth-quarter profit of $260 million, and a profit of $2.94 billion for all of 2008. It also had a credit-loss provision $1.3 billion in the fourth quarter, compared with actual charge-offs of $627 million. U.S. Bancorp is in good shape, with no apparent need for extra money.

7. **The Bank of New York Mellon Corp. (BK) -** ***Hidden Gem***: New York Mellon has $237 billion in assets, mostly through its operations in New York and Pennsylvania. It received $3 billion in TARP funding. With closing price Friday at $25.26, Bank of New York Mellon was trading at 125% of its book value (the shares closed yesterday at $23.13, down 8.4%). The bank posted a fourth-quarter profit of $28 million, and net income of $1.39 billion for all of 2008. The fourth quarter was tough as for everybody, but Bank of New York Mellon appears to have no near-term need for funding.

8. **SunTrust Banks Inc. (STI)** - ***Walking Wounded***: Sun Trust has $189 billion in assets, and received $4.9 billion in TARP financing. Based in Atlanta, the bank has operations in the Mid-Atlantic and the Southeast. Its Friday closing price of $8.72 meant that SunTrust shares were trading at only 19% of their book value. The company posted a fourth-quarter loss of $379 million, but a profit of $747 million for all of 2008. It also had loan-loss provisions $962 million in the fourth quarter, compared with $552 million in charge-offs. SunTrust has reduced its quarterly dividend sharply to 10 cents per share, but it appears to be in no immediate trouble. However, if the economy deteriorates, the bank's exposure to the Florida housing market could be an Achilles heel. Investors are clearly concerned: SunTrust shares took an 18% beating yesterday, and are down 88% in the past year, ***The Atlanta Journal-Constitution*** reported yesterday.

9. **State Street Corp. (STT) -** ***Hidden Gem***: State Street had $174 billion in assets, and received $2 billion in TARP funding. It's a Boston-based bank, but serves institutional investors throughout the world. At Friday's closing price of $27, the shares were trading at 111% of their book value. State Street posted fourth-quarter earnings of $65 million, and 2008 earnings per share of $3.89, up 13% from the year before. With a global business, conservative leverage and Boston management, State Street could gather strength when the financial crisis finally ends.

10. **Capital One Financial Corp. (COF)** - ***Walking Wounded***: Capital One has $161 billion in assets, and received a $3.6 billion TARP investment. It's primarily a credit card company, headquartered in McLean VA. At Friday's close of $12.11, it is trading at just 20% of book value. Capital One lost $1.4 billion in the fourth quarter of 2008, and was just below break-even for the full year, but made $895 million from continuing operations. Its stock pays a quarterly dividend of 37.5 cents per share. Capital One is in dangerous waters and could soon succumb to zombification if credit-card problems

really escalate.

11. **BB&T Corp. (BBT)** - ***Hidden Gem***: BB&T has $152 billion in assets, and accepted a $3.1 billion TARP investment. It's a regional bank, headquartered in Winston-Salem NC, with its primary operations in the Mid-Atlantic region. At Friday's closing price of $15.33 a share, the stock was trading at about 58% of its book value. The company posted net earnings of $284 million in the fourth quarter, after loan write-offs of $528 million. It posted a profit of $1.5 billion for all of 2008, and pays a quarterly dividend of 47 cents a share. I'm sure it would gladly take more taxpayer money, but it certainly doesn't appear to need it.

12. **Regions Financial Corp. (RF)** - ***Walking Wounded***: Regions has $146 billion in assets, and received $3.5 billion in TARP financing. It's a regional bank, headquartered in Birmingham, AL, with operations primarily in the Southeast. At Friday's closing price of $3.38 a share, Regions' stock was trading at about 18% of book value, and the bank has suspended its dividend. The company lost $5.6 billion in 2008, and its tangible net worth is only $10.5 billion. However, on an operating basis, it made a profit of about $300 million. Regions had a fourth-quarter loan-loss provision of $1.15 billion, and charge-offs of $796 million. I'm classifying it as "walking wounded," but think it's more likely to revive itself than to accept a toe-tag. In fact, it's likely to need only a modest amount of additional funding to see its health improve.

And the Winners Are …

After examining the finances of these 12 major banks, I discovered that some additional analysis was needed - some in the investment arena, and the rest in the area of public policy. Once that was completed, I was able to reach some concrete conclusions about the new banking bill.

On the public policy side, it's very difficult to justify $1.5 trillion of public money being used to buy assets from these guys. Of 12 banks I examined:

- Seven appear to be in solid shape, and are actually paying substantial dividends.
- Three appear weak, with possible needs for some additional help.
- And only two are actual basket cases.

Apart from the two dogs, all these banks have shown themselves perfectly capable of handling the difficult parts of their asset portfolios. That means that setting up a separate state bureaucracy to manage them, instead. is just asking for a high-cost taxpayer rip-off.

Unless it's proposed to devote $1.5 trillion of taxpayer money to the apparently hopeless task of sorting out Bank of America and Citigroup, the true need is much smaller, with the remaining $315 billion from the original TARP program probably being more than ample for the other U.S. banks.

The most likely near-term need would appear to be capital injections into one or two of the weaker members of this Group of 12. As for the true bow-wows, the best solution from a public-policy and taxpayer-protection viewpoint would be to allow Bank of America and Citigroup to slide into Chapter 11 re-organization, with the ultimate objective being a breakup and sell-off of the worthwhile pieces, while holding back the relatively modest amounts of government financing or Federal Reserve money that might be needed to staunch any blood-letting that their bankruptcy caused.

As investments, the "***Hidden Gems***" for the most part represent very interesting potential bargains.

USB looks solid and profitable, with a dividend yield of an extraordinary 15.84% as of yesterday's close.

BNY Mellon does not appear particularly risky, but yields only 4%; I actually prefer the "***Risky-but-Proud***" PNC, which has considerable upside if it can manage to digest its National City acquisition, avoid big credit losses and achieve cost savings.

State Street has a dividend yield of only 4.14%, but looks rock solid and its shares are trading at only about 5.9 times earnings.

BBT also looks solid, and has a massive dividend yield of 13.18%.

If you think the U.S. economy is descending into a bottomless pit, hold off. But if you're reasonably optimistic long-term, these banks are well worth considering for income-oriented investors.

[Editor's Note: When it comes to either banking or the international financial markets, there's no one better than ***Money Morning*** **Contributing Editor Martin Hutchinson, for he brings to the table the kind of high-level expertise that our readers have come to expect. In** February 2000, for instance, when he was working as an advisor to the Republic of Macedonia, Hutchinson figured out how to restore the life savings of 800,000 Macedonians who had been stripped of nearly $1 billion by the breakup of Yugoslavia and the Kosovo War.

Hutchinson warned ***Money Morning*** readers about the dangers of credit-default swaps back in April - long before the collapse of American International Group Inc. (AIG) made those derivative securities a household word. And his recent analysis of how the U.S. stock market would respond to the credit crisis proved to be incredibly accurate. Hutchinson is also a regular contributor to our monthly investment newsletter, ***The Money Map Report****, which details profit plays as well as the kinds of risk-management strategies that keep investors from losing money in the whipsaw markets spawned by the global credit crisis.*

That crisis has eradicated trillions of dollars in shareholder wealth, making the investment equation tougher than ever for U.S. investors who are trying to "dig out" after a decade of losses. The uncertainty surrounding the economic-stimulus and banking-bailout plans isn't helping. But a new ***Money Morning*** report is a two-way win for investors: It addresses the bear-market threats these plans pose, and also spotlights some of the hard-to-find but potentially lucrative profit plays that remain. The report is free of charge, and also details ways that readers can obtain a copy of ***The New York Times*** best seller, **"Crash Proof," in which author and frequent *Money Morning* contributor Peter D. Schiff details the causes of the housing bubble and financial-system collapse, and tells investors how to dodge losses from the problems that are still to come.** To read our free report, and to find out more about this offer, please click here.**]**

News and Related Story Links:

- **Money Morning News:**
  Bank of America, Wells Fargo and PNC End 2008 by Closing Major Buyout Deals.

- **About.com**:
  Price-to-Book Ratio.
- **Wikipedia**:
  Troubled Assets Relief Program.
- **Money Morning News**:
  JPMorgan Chase Biggest U.S. Bank With Its Purchase of Failed WaMu.
- **Money Morning News**:
  Citigroup Concedes Wachovia to Wells Fargo.
- **The Atlanta Journal-Constitution**:
  SunTrust's stock price plunges 18%.
- **Money Morning Banking Bailout Investigative Report**:
  Obama Administration Must Revive "Shadow Financial System" to Revive U.S. Banks.
- **Money Morning News Analysis**:
  Geithner Unveils TARP Overhaul.
- **Money Morning News**:
  Obama Requests Release of Second Half of $350 Billion TARP.
- **Money Morning News Analysis**:
  The New Banking Bailout Plan Reconstitutes Some of the Same Ingredients That Touched Off the Financial Crisis

This entry was posted on Wednesday, February 18th, 2009 at 2:50 pm and is filed under Main Essay. You can follow any responses to this entry through the RSS 2.0 feed. Due to the amount of comments we receive Money Morning will not be able to respond to all questions. If you have not already registered to leave a comment, once doing so you will receive Money Morning's Daily Email.

There Are 4 Responses So Far. »

1. *Comment by vijay gopal* on 18 February 2009:

   Will AIG be a good investment at this time? I understand that except for a couple of grey areas, the company is otherwise solid.

   thanks

2. *Comment by Lewie White* on 18 February 2009:

   I agree that giving taxpayers money away, escpecially to large corporations is only delaying the inevitable. At which point we will lose all investment. just like the Auto industry. The money needs to be put into the hands of the people who will need to spend it. Small businesses and individuals. I am not talking about 3- 6 hundred either. Psolpe are not going to put hard earned money into anything if tey think they may not have a job next week. I personally will not purchase anything major such as a car even though mine is more than six years old. For one the vehicles need to be more fuel and energy concious and the oil industry needs to be reeled in. With the rising prices of everthing people are having trouble just making it from week to week. giving money to these large corporatians is not creating any jobs or even helping to keep the status Quo.

3. *Comment by nunya* on 18 February 2009:

   Are you kidding me about BB&T “gladly [taking] more taxpayer money”? You are an idiot if you don’t the former and present CEOs’ philosophy? Does Ayn Rand ring a bell? Do some more research.

4. *Comment by nunya* on 18 February 2009:

   *don’t know

Post a Response

Name (required)

Mail (will not be published) (required)

Website

Submit Comment

-
- # Top News Stories

- 02/18/2009
  Obama Signs Stimulus Bill Today, Announces Foreclosure Plan Tomorrow
- 02/17/2009
  Sirius Business – Liberty Injects $530 Million into Satellite Radio Provider
- 02/14/2009
  China's Stimulus Ignites Economy
- Premium
  Bailout Bombshell Could Crush Investors
- Feature
  Jim Rogers Reveals: 150 Companies Poised to Beat the Crisis
- Feature
  IBM: Buy, Sell or Hold?

More Top Stories...

Money Morning RSS Feed

$

Buy, Sell or Hold?

By Horacio Márquez

See our latest stock reports...

Weekly Economic Calendar

Date	**Release**
February 16	Presidents' Day
February 18	Housing Starts (01/09)
	Industrial Production (01/09)
February 19	PPI (01/09)
	Initial Jobless Claims (02/14/09)
	Leading Indicators (01/09)
February 20	CPI (01/09)

-

- ## Investor Reports
  - Retirement Blues: Financial Crisis Pulls Billions From Pension Plans, Crimping Consumers' Dreams and Corporate Profits.
  - The Five Most Promising Emerging Market ETFs for 2009

- [The "Cheap Oil Era" is Ending Soon…]

- Legal / Disclaimers
- Privacy Statement
- Contact