Investing In Community Banks Stocks To Fly

by Steve Brown

The futuristic age seems to be upon us. In fact, Uber recently announced a ground-breaking project of flying cars called Uber Elevate. They hope to have these flying cars available in the next 10Ys. Consider all of the hours of productivity lost in traffic. That is where Uber's VTOL (vertical take-off and landing) electric flying vehicles could be a transportation game-changer. VTOL can reportedly fly both horizontally and vertically, making it easier to pick up people in urban areas using helipads. Knowing that the Saudi Investment Fund recently invested $3.5B into Uber definitely builds some creditability in getting such a revolutionary project done. However, it is still a pretty wild investment. This leads us to the future of community bank investing.

Talking heads on TV will regularly discuss how financial stocks are doing, what about community bank stocks? There is rarely news about those, because most are privately held or infrequently traded so it is tough to easily discern trends.

On the good news front - Tim Melvin (a former stockbroker, investor and columnist for the website, Real Money) says investing in community banks is "the trade of the decade." He indicates small bank stocks are somewhat "counter-intuitive," as many investors are looking for banks that are having a hard time performing for reasons outside of their control. In other words, if you are one of those banks grappling with industry and regulatory pressures, you may be in luck. Melvin suggests that regulatory compliance and its drag on profits - within a low interest rate environment - demands efficiency and as such is driving merger and acquisition activity.

To shed more light on this subject, we looked at a Community Banking in the 21st Century Research and Policy Conference survey. It found 10% of banks mentioned receiving and seriously considering an acquisition offer while 20% of banks made an acquisition offer. Reasons were unsurprisingly focused on expansion and market entry or growth.

This still leaves up to 90% of banks working every day in the salt mines trying to generate business. To the broader industry, we note that a consolidating market is not the only reason investors are finding community bank stocks attractive.

For one, heavy regulation has pushed down the risk profile of the industry, so investors can get solid returns without taking on too much risk. That increases investor interest in bank stocks.

Another is that community banks are doing quite well supporting their communities. Many banks are doing just fine and are reporting strong loan growth. While NIM can be challenging and technological changes expensive, many banks have been quite effective managing things as profitability increases. As above, these factors also help raise investor interest.

Still another reason can be that many community banks pay good dividends. These can be beneficial to have in any portfolio and can make for a good trade off to a lower level of liquidity.

One more reason investors should like community bank stocks is that these banks truly support local communities. For investors living in those communities, this can be important, as it helps ensure local areas thrive and that lending is robust.

Finally, consider that community banks usually have financial statements that are very straightforward. The basic model is to take deposits and then use that money to make loans to small businesses operating in their community. That makes it easy for investors to understand and value.

BANK NEWS

New Services

Research by Fiserv finds top areas people said they would like to see banks add or improve are: same day posting of transactions (33%), identity protection service (31%), a calendar view of billing and payments including upcoming weeks (21%), account balance with pending payments deducted (19%), transfer money between their accounts at different financial providers (16%), additional payment option of paying other people (14%) and budget information about financial transactions (13%).

Online Spending

Reuters reports $3.45B was spent on Cyber Monday, a 12.1% increase over last year.

Industry FIs

FDIC research finds the total number of commercial banks and savings institutions declined from 6,058 in Q2 to 5,980 as of Q3 of this year. This is just over a 1% decline for the quarter, which is in line with historical trends (1% per quarter and 4% per year). At this pace, the total would dip below 5,000 as of Q1 of 2020.

Rate Hike

Fed Governor Powell said the case for a rate hike has "clearly strengthened" over the previous few weeks. For their part, investors continue to anticipate a 25bp rate hike at the Dec FOMC meeting.

Loan Growth

FDIC research finds total loans and leases grew 1.2% from Q2 to Q3, or about 4.9% annualized.

Digital Disruption

Research by MIT finds 90% of financial services firms agree or strongly agree that digital technologies are disrupting the industry to a moderate or great extent.

Loans to Assets

Fed research finds the net loan and lease to asset percentage nationwide was 65% in Q3. This compares to only 59% for the same period in 2012 and a high reached in Q3 2008 of 67%.

Biometrics

Research by Deloitte finds 31% of those surveyed ages 18 to 24Y say they are using fingerprint scanners on their phones vs. only 8% of those over age 65.