



## Increasing Shareholder Value in Today's Economic Environment

by [Steve Brown](#) [economy](#) [board of directors](#) [management](#)

**Summary:** Banks should be benefiting from the interest rate increase, but bank stock prices aren't following the trend. There are actually many other factors that impact bank stock prices that are keeping current share prices down. Here are the root causes of the current prices and what CFIs can do to turn the market in their favor as rates continue to rise.

In a scene from 1985's "Back to the Future," the electrical wires that Doc is setting up on the clock tower disconnect while Marty speeds down the street toward the time travel setup. With seconds left, Doc ziplines down the cords to get to the disconnected line just in time for the lightning strike. Marty's car runs over the electrified lines and disappears, just as planned, without him knowing he almost missed his journey.

Much like Doc's nearly failed endeavor, things don't always go according to plan. Sometimes, it takes some quick thinking and adaptability to get where you need to be. That's exactly the case with the current stock landscape.

With interest rates up dramatically YoY, financial institutions can charge more on both consumer and commercial loans. That should make institutions more profitable and push individual bank stock prices higher.

Yet that isn't what has happened. Why haven't bank stocks benefited from higher interest rates? What can community financial institutions (CFIs) do to improve their own value to shareholders?

### Bank stocks trend downward as interest rates trend upward

The federal funds rate stood at [a quarter of a percent as 2022 began](#). In response to growing inflation, the Federal Reserve raised rates by a quarter percent on March 16; half a percent on May 4, when Russia invaded Ukraine and China brought back COVID-19 restrictions; and three-quarters of a percent on June 15, when inflation stood at a 40Y high. We are expecting another rate hike this month.

Residential mortgages responded with both increases and volatility. Mortgage rates for a fixed, 30Y loan went as high as 5.81% in June 2022. By July 14, the average 30Y fixed mortgage rate was 5.51%, a YoY increase of 2.63%.

The [NASDAQ bank index](#) tells a different story. From the beginning of the year to July 14, the index lost 65.56 points, or 1.65%.

### What affects bank stock prices?

Interest rates affect bank stock prices, but they are far from the only factor in the mix. Other concerns include overall market sentiment, demand for banking services, and the outlook for economic and bank growth.

At a more individual level, three kinds of risk — interest rate risk, regulatory risk, and counterparty risk — can all influence a financial institution's share value. So can a bank's price-to-earnings and price-to-book ratios.

## Why haven't stock prices gone up in step with interest rates?

The answer to this question lies in the complicated current economic climate. Bank profits do generally rise with interest rates. But higher interest rates also mean that fewer customers can afford to make loan payments on a given principal amount.

Economic downturns also reduce the number of potential borrowers who can qualify for a loan, because some would-be customers lose jobs and therefore can't qualify for a loan, and others see their incomes drop. Even customers who could qualify for a loan become less confident about their incomes and therefore less likely to take the financial risk that a loan represents. Banks' risk of loan loss goes up as well.

In other words, during an economic downturn banks write a smaller number of loans, albeit at a higher interest rate, and average loan quality falls. That's the kind of mixed news that doesn't necessarily send equity value soaring.

## What can CFIs do to improve shareholder value?

The economic environment matters to your institution and its share price, but so do the specific actions you take. To improve shareholder value, consider:

- **Determining your shares' fair market value.** It's relatively simple to determine fair market value of publicly traded shares at any given moment, or by taking the average of the price on a specific day. It's also helpful when the shares trade on an established public market, such as OTCQX or OTCQB. Privately held CFIs will need to call multiple investors to get a sense of market value.
- **Reducing the risk of owning or trading your CFI's shares.** Explore the possibility of trading on an established, public market. This style of trading offers transparent pricing, liquidity access, and readily available news and financial disclosure, all which raise share value. The most popular two public markets, OTCQX and OTCQB, also have standards that let them verify that banks are meeting standards and putting risk controls around their shares. (The Pink exchange, by contrast, does not offer verification.)
- **Finding ways to publicize your news and disclosures.** Trading on a public market is one way to make sure that broker-dealers and investors see your news and disclosures.
- **Establishing liquidity through a walk-in repurchase program or a voluntary stock repurchase program,** if you choose not to trade your CFI shares on a public exchange.

Deliberately adding liquidity, reducing risk, and publicizing disclosures and news can all increase your CFI share value, even in a challenging economy.

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## ECONOMY & RATES

Rates As Of: 08/02/2022 01:18PM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	2.56	0.15	2.50
6M	3.00	0.09	2.81
1Y	3.08	0.15	2.69

2Y	3.07	0.18	2.33
5Y	2.86	0.18	1.60
10Y	2.76	0.11	1.25
30Y	3.02	0.01	1.12
<b>FF Market</b>	<b>FF Disc</b>	<b>IOER</b>	
2.33	2.50	2.40	
<b>SOFR</b>	<b>Prime</b>	<b>OBFR</b>	
2.28	5.50	2.32	

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