Banks: a phoenix from the flames?

John Bailer,
U.S. equity income manager, Mellon, a BNY Mellon company

BNY MELLON | Dreyfus

Ten years ago, it may have felt like the world was going to end. The financial system appeared broken and banks were to blame. Valuations in the sector fell dramatically and we saw government bailouts around the globe.

A decade on and things have changed. U.S. regulators have imposed higher capital requirements and financial services companies have been forced to raise their game.

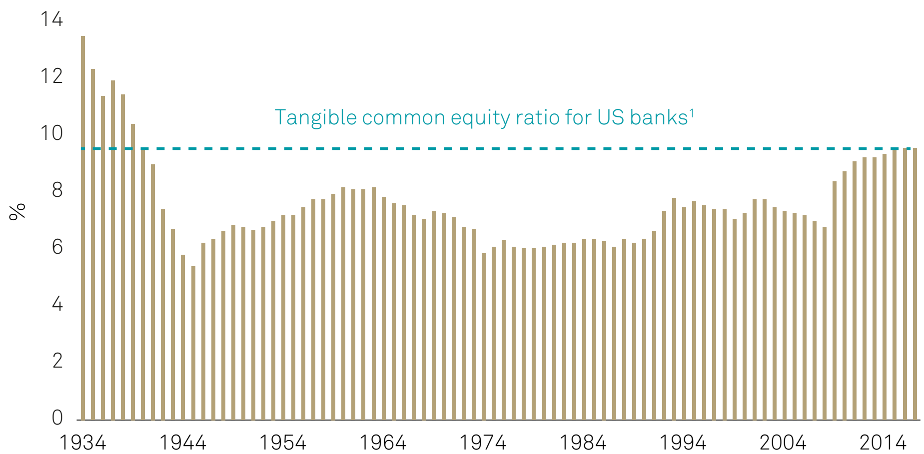
As a result, the banking sector appears to be in much better shape and now looks very different indeed. For one thing, the U.S. is not facing the same national housing issue it was 10 years ago, so financial services have less leverage and more liquidity than they have had in decades.

In this sense, the global financial crisis (GFC) provided an opportunity to get things right. We believe the U.S. banking sector now looks more resilient than ever: it has not only survived previous downturns but has stood tall. In 2016, for instance, when the oil price collapsed, investors worried about energy-related defaults and collateral damage to financials that never came. There was a widespread (and unnecessary, in our view) preoccupation with 2008/09.

Looking forward, we believe the sector offers growing dividend yields, good capital return prospects and a measure of downside protection at what we believe are compelling valuations.

> **The global financial crisis provided an opportunity to get things right.**

U.S. BANK BALANCE SHEETS IN BETTER SHAPE



Source FDIC and NYFRB, 1934 – 2017. As at December 31, 2017.

CCAR: SEVERE ADVERSE SCENARIO TESTS[2]

Scenario	U.S. Bank Results
Real GDP declines 8.9%	PASS
Market declines 65%	PASS
Unemployment increases to 10%	PASS
Home prices fall 30%	PASS
Commercial real estate declines 40%	PASS
3 Month Treasury yield declines to 0.1%	PASS
10 Year Treasury yield declines to 0.7%	PASS

Source: U.S. Federal Reserve, June 28, 2018.

1 A Tangible Common Equity Ratio is used to try and estimate a how much a bank can sustainably lose before shareholder equity starts to become affected. The higher the TCER, the more robust banks' balance sheets are deemed to be.

2 The Comprehensive Capital Analysis and Review (CCAR) is an annual exercise by the Federal Reserve to ensure that institutions have well-defined and forward-looking capital planning processes that account for their unique risks and sufficient capital to continue operations through times of economic and financial stress. In the most recent test in June 2018 all 35 lenders assessed were found to be able to withstand a severe economic downturn.

MARK-45299-2018-12-27

BNY MELLON | Dreyfus