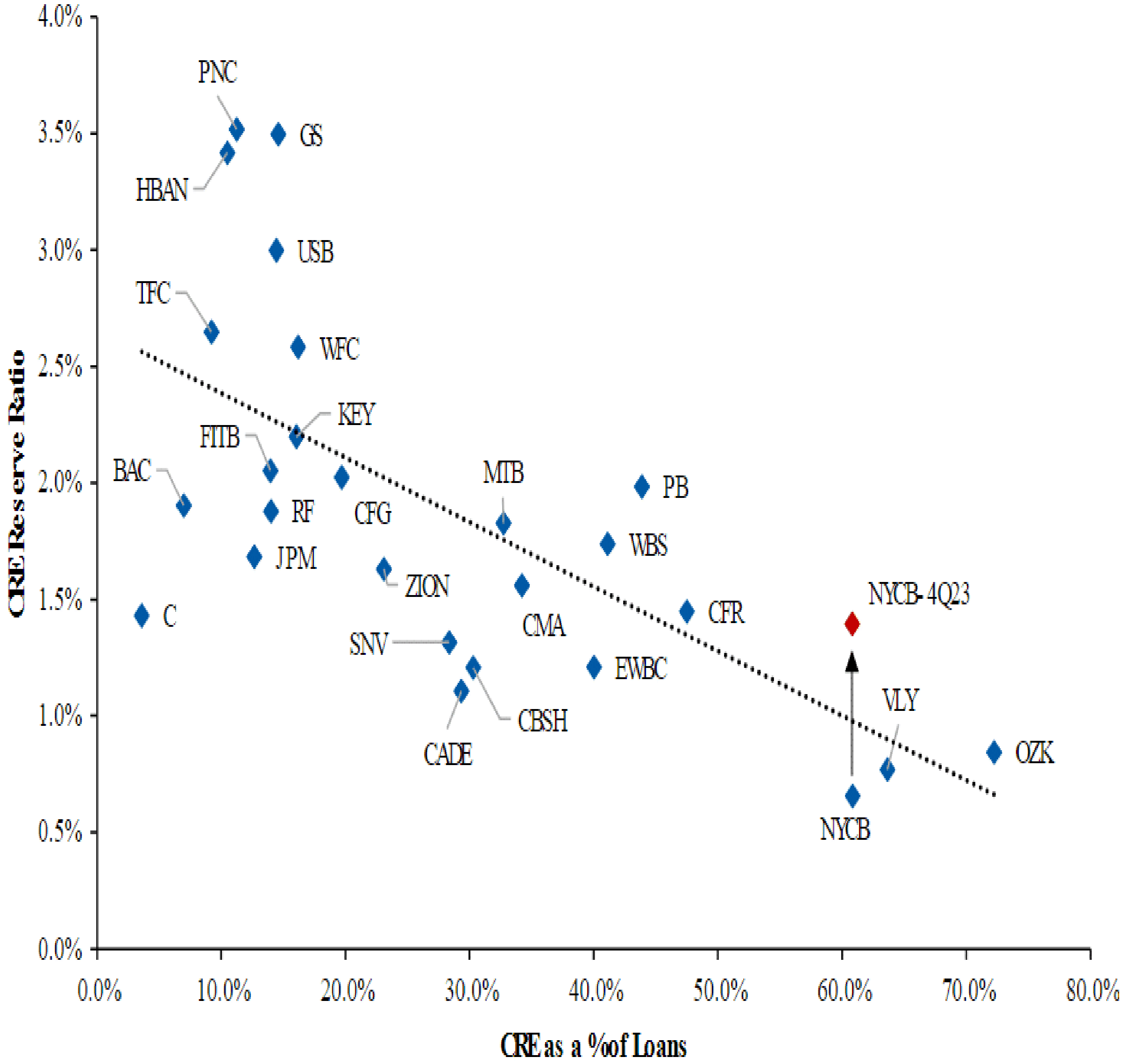
CRE Contagion - Which Banks Are At Risk?

The price of New York Community Bank (NYCB) was cut in half last week as it drastically increased its loan loss reserves. As we noted in a recent Commentary, they took this action partly because of the commercial real estate (CRE) loans they bought from the failed Signature Bank. The work-from-home movement and higher interest rates are crushing CRE values. As a result, the banks that made CRE loans may be on the hook if the borrower fails. On Sunday?s 60 Minutes, Powell admits CRE may be problematic for smaller banks. Regarding CRE, he stated:

> *We looked at the larger banks? balance sheets, and it appears to be a manageable problem. There?s some smaller and regional banks that have concentrated exposures in these areas that are challenged.*

To help us better assess bank risks, we share a chart from Morgan Stanley. The graph compares the loan loss reserves banks hold for CRE loans versus their overall exposure to said loans. NYCB has high exposure to CRE. Furthermore, before last week?s action, they did not have adequate loan loss reserves. In general, CRE constitutes less than 20% of the larger bank holdings. However, we offer caution for smaller banks with 30% or more exposure and low loan loss reserves. This includes banks like ZION, CADE, VLY, and CBSH.

Exhibit 7: Banks with a higher exposure to CRE tend to have a lower CRE reserve ratio (Data as of 3Q23. NYCB shown for both 3Q23 & 4Q23).



Note: Data is sourced from Bank Call Reports. Includes reserves on construction & development loans. Source: Company data, Morgan Stanley Research

What To Watch Today

Earnings

Time	Symbol	Company Name	Market Cap ▾	Fiscal Quarter Ending	Consensus EPS* Forecast	# Of Ests	Last Year's Report Date	Last Year's EPS*
	LLY	Eli Lilly and Company	$626,950,978,531	Dec/2023	$2.46	8	2/02/2023	$2.09
	TM	Toyota Motor Corp Ltd Ord	$278,569,700,535	Dec/2023	$3.66	1	2/09/2023	$3.78
	LIN	Linde plc	$198,150,497,103	Dec/2023	$3.50	6	2/07/2023	$3.16
	AMGN	Amgen Inc.	$173,697,380,443	Dec/2023	$4.66	11	1/31/2023	$4.09
	UBS	UBS AG	$102,104,600,000	Dec/2023		N/A	1/31/2023	$0.50
	BP	BP p.l.c.	$99,672,753,149	Dec/2023	$1.09	5	2/07/2023	$1.59
	GILD	Gilead Sciences, Inc.	$97,390,634,513	Dec/2023	$1.76	12	2/02/2023	$1.67
	FI	Fiserv, Inc.	$86,390,731,961	Dec/2023	$2.15	15	2/07/2023	$1.91
	KKR	KKR & Co. Inc.	$78,013,514,789	Dec/2023	$0.82	4	2/07/2023	$0.72
	CMG	Chipotle Mexican Grill, Inc.	$67,020,408,613	Dec/2023	$9.73	15	2/07/2023	$8.29
	FTNT	Fortinet, Inc.	$51,027,593,119	Dec/2023	$0.37	13	2/07/2023	$0.38
	F	Ford Motor Company	$48,435,748,687	Dec/2023	$0.13	5	2/02/2023	$0.51
	EW	Edwards Lifesciences Corporation	$47,737,615,000	Dec/2023	$0.64	13	1/31/2023	$0.64
	CARR	Carrier Global Corporation	$46,642,599,326	Dec/2023	$0.51	7	2/07/2023	$0.40
	SPOT	Spotify Technology S.A.	$42,323,494,180	Dec/2023	($0.08)	9	1/31/2023	($1.43)
	CNC	Centene Corporation	$40,225,335,300	Dec/2023	$0.43	7	2/07/2023	$0.86
	CTSH	Cognizant Technology Solutions Corporation	$39,050,009,082	Dec/2023	$1.04	9	2/02/2023	$1.01
	AME	AMTEK, Inc.	$38,282,573,236	Dec/2023	$1.62	7	2/02/2023	$1.52
	PRU	Prudential Financial, Inc.	$37,071,090,000	Dec/2023	$2.67	8	2/07/2023	$2.42
	IT	Gartner, Inc.	$36,402,781,290	Dec/2023	$2.78	4	2/07/2023	$3.70
	CMI	Cummins Inc.	$34,439,749,363	Dec/2023	$4.41	9	2/06/2023	$4.52
	GEHC	GE HealthCare Technologies Inc.	$33,847,315,116	Dec/2023	$1.07	5	1/30/2023	$1.31
	XYL	Xylem Inc.	$27,815,554,256	Dec/2023	$0.96	7	2/07/2023	$0.92
	DD	DuPont de Nemours, Inc.	$26,645,432,804	Dec/2023	$0.85	4	2/07/2023	$0.89
	SNAP	Snap Inc.	$26,128,296,346	Dec/2023	($0.16)	8	1/31/2023	($0.08)
	WTW	Willis Towers Watson Public Limited Company	$25,534,233,442	Dec/2023	$7.04	11	2/09/2023	$6.33
	TW	Tradeweb Markets Inc.	$22,361,280,769	Dec/2023	$0.63	10	2/02/2023	$0.47
	CHKP	Check Point Software Technologies Ltd.	$19,562,231,682	Dec/2023	$2.16	13	2/13/2023	$2.23
	WAT	Waters Corporation	$19,183,747,687	Dec/2023	$3.56	8	2/15/2023	$3.84
	VLTO	Veralto Corp.	$18,913,995,697	Dec/2023	$0.80	3	N/A	N/A
	OMC	Omnicom Group Inc.	$17,776,467,807	Dec/2023	$2.16	3	2/07/2023	$2.09
	CINF	Cincinnati Financial Corporation	$17,349,286,600	Dec/2023	$1.92	10	2/06/2023	$1.27
	J	Jacobs Solutions Inc.	$17,259,046,099	Dec/2023	$1.50	5	2/07/2023	$1.67
	ATO	Atmos Energy Corporation	$17,194,364,345	Dec/2023	$2.09	3	2/07/2023	$1.91
	IEX	IDEX Corporation	$16,651,231,177	Dec/2023	$1.78	6	1/31/2023	$2.01
	CSL	Carlisle Companies Incorporated	$15,531,953,212	Dec/2023	$3.42	3	2/07/2023	$3.92
	ESS	Essex Property Trust, Inc.	$15,250,261,910	Dec/2023	$3.81	13	2/07/2023	$3.77
	YUMC	Yum China Holdings, Inc.	$14,672,316,956	Dec/2023	$0.13	4	2/07/2023	$0.13
	ENPH	Enphase Energy, Inc.	$14,397,960,215	Dec/2023	$0.24	15	2/07/2023	$1.13
	AMCR	Amcor plc	$13,672,946,785	Dec/2023	$0.15	3	2/07/2023	$0.19
	AZPN	Aspen Technology, Inc.	$13,026,782,756	Dec/2023	$1.23	3	1/25/2023	$0.06
	JKHY	Jack Henry & Associates, Inc.	$12,138,276,427	Dec/2023	$1.14	6	2/07/2023	$1.10

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Economy

Time	Event	Impact	Actual	Dev	Consensus	Previous
TUESDAY, FEBRUARY 6						
00:00	USD Fed's Harker speech			SPEECH		
13:55	USD Redbook Index (YoY)(Feb 2)		-	-	-	5%
15:00	USD RealClearMarkets/TIPP Economic Optimism (MoM)(Feb)		-	-	47.2	44.7
17:00	USD Fed's Mester speech			SPEECH		

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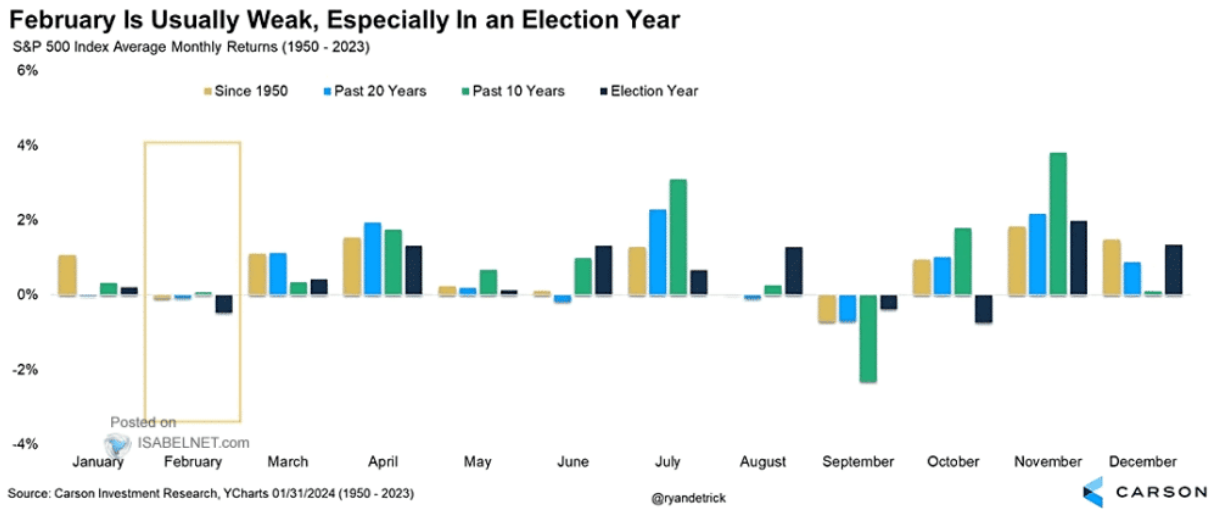
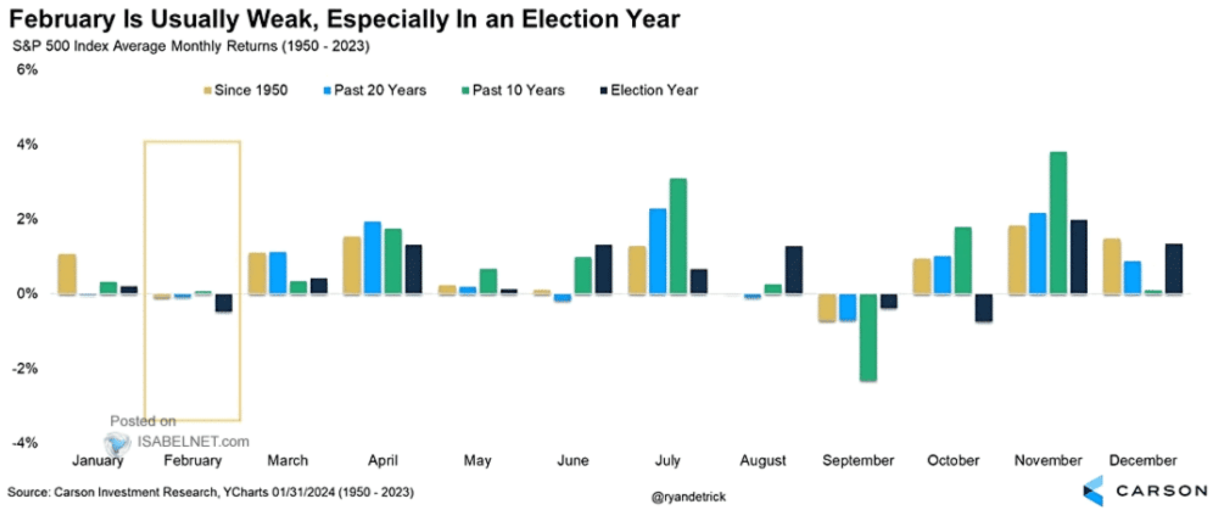
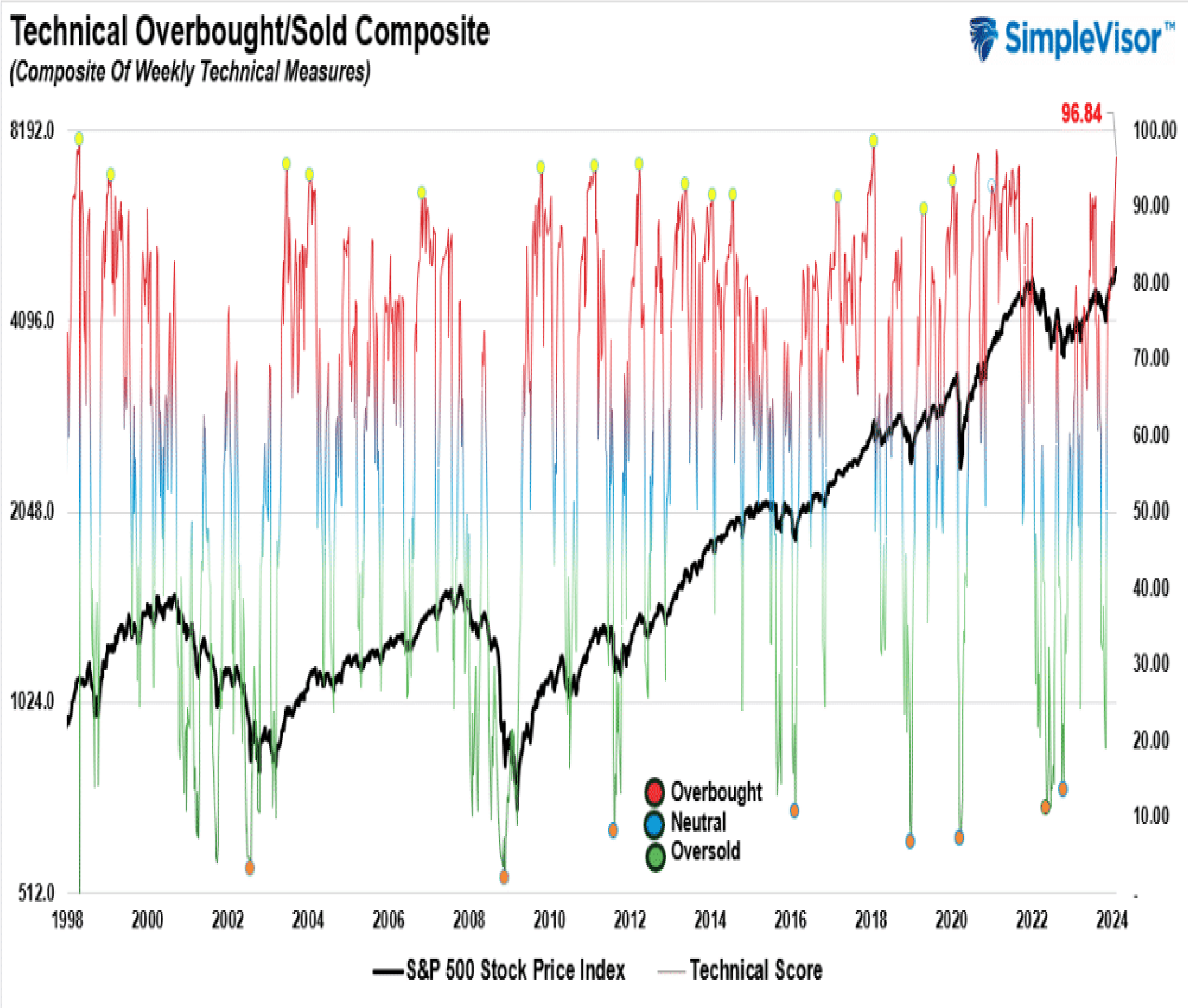
Market Trading Update

The market stumbled out of the gate yesterday, trading a bit weaker following last week?s surge to new highs. Currently, the market is just a ?stone?s throw? from the psychological level of 5,000, which is most likely inevitable at this juncture. As noted ***in yesterday?s commentary***, we continue to expect a correction to resolve current overbought conditions, and the month of February tends to trade weaker particularly when following a very strong January advance.





While the market remains in a strongly bullish trend, such does preclude the market from some type of corrective activity to reduce more extreme overbought conditions, as shown in our weekly composite technical gauge. Readings above 90 have historically preceded short-term corrective actions and broader market declines.


Technical Overbought/Sold Composite
(Composite Of Weekly Technical Measures)
SimpleVisor™
96.84
8192.0
4096.0
2048.0
1024.0
512.0
100.00
90.00
80.00
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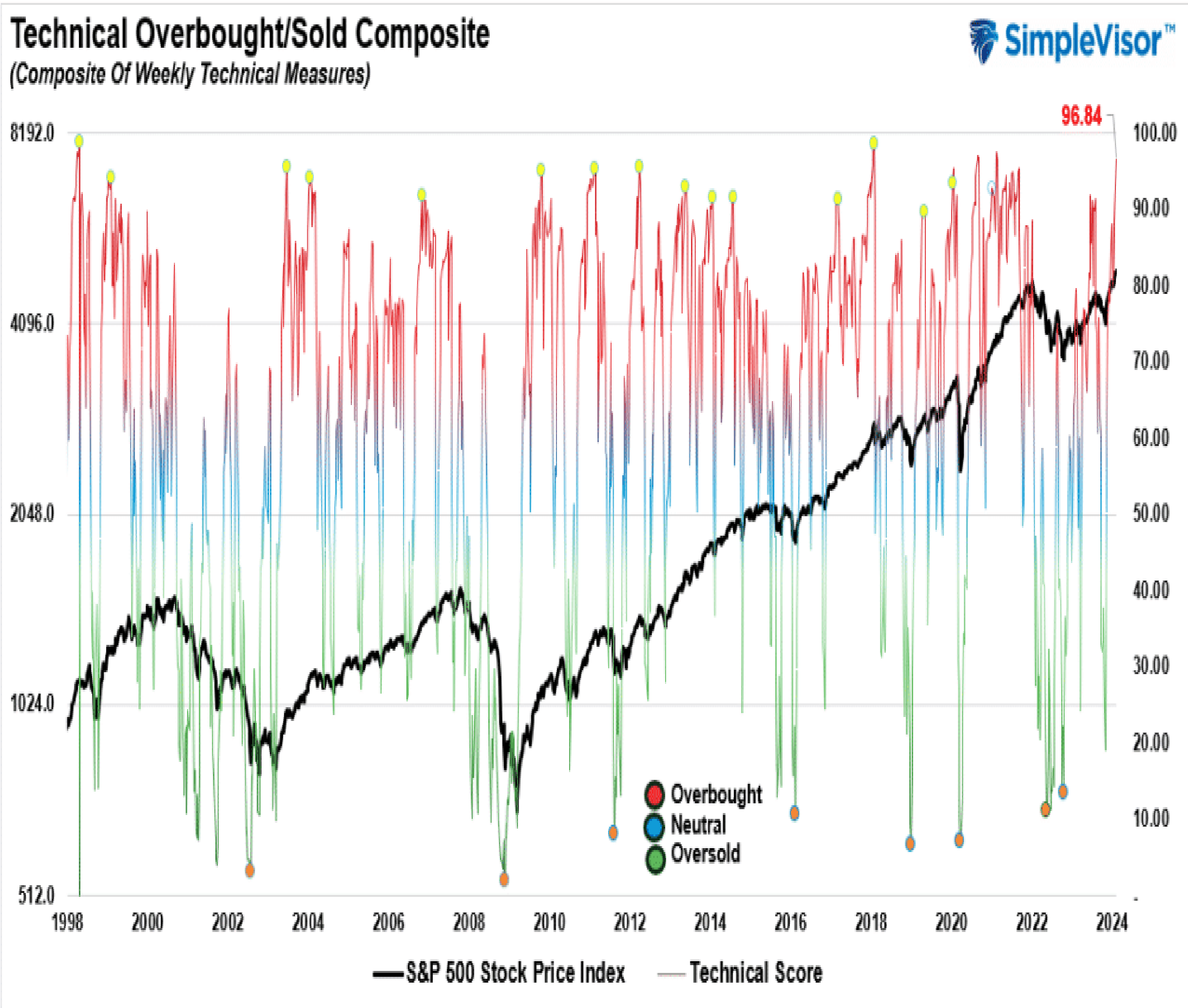
2024
Overbought
Neutral
Oversold
S&P 500 Stock Price Index
Technical Score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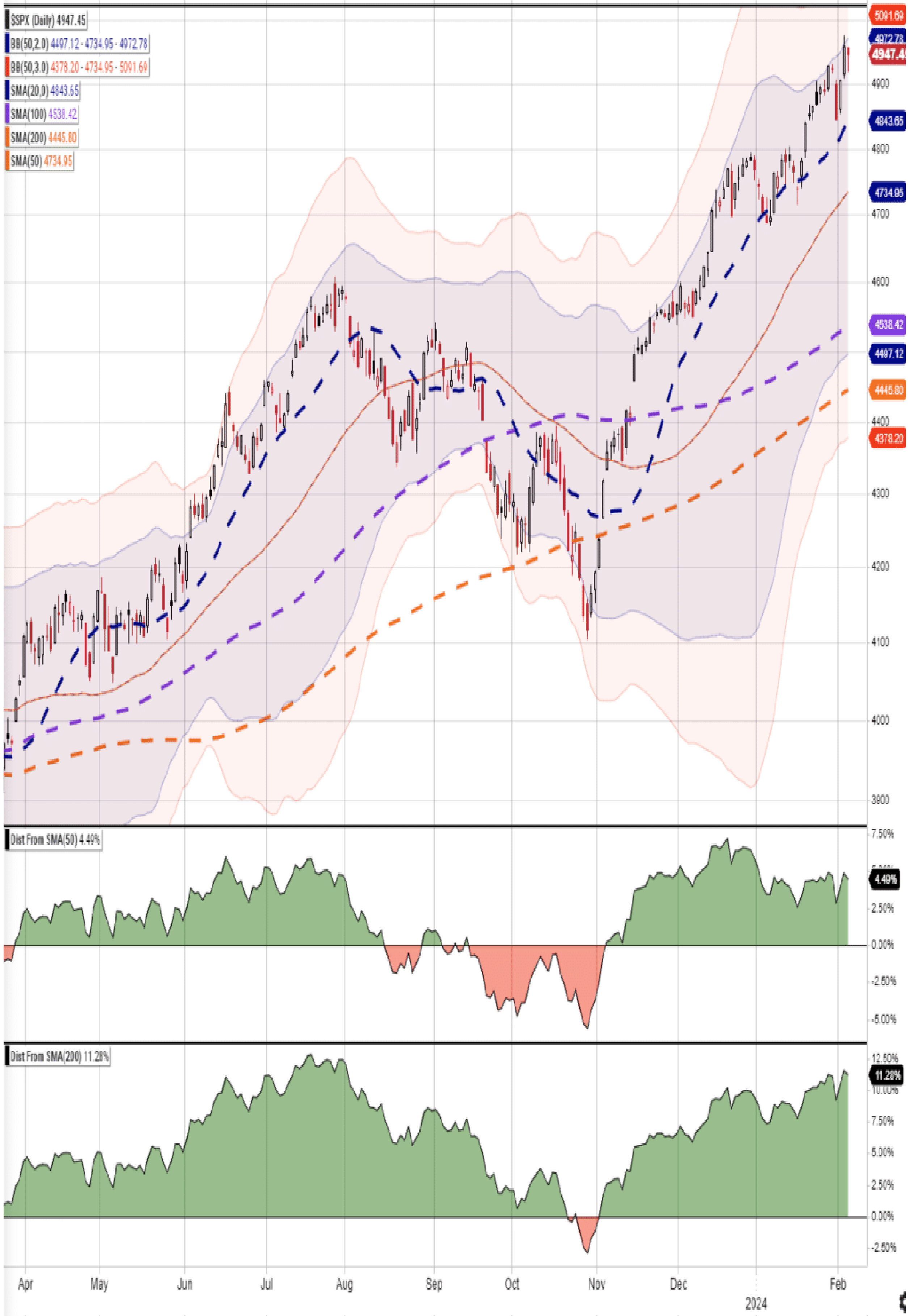
Overbought
Neutral
Oversold
S&P 500 Stock Price Index
Technical Score

With the market overbought, pushing into 2-standard deviations above the 50-DMA, and well deviating above the 50- and 200-DMA, the conditions for a short-term reversal are present.


$SPX (Daily) 4947.45
BB(50,2.0) 4497.12 - 4734.95 - 4972.78
BB(50,3.0) 4378.20 - 4734.95 - 5091.69
SMA(20,0) 4843.65
SMA(100) 4538.42
SMA(200) 4445.80
SMA(50) 4734.95
Dist From SMA(50) 4.49%
Dist From SMA(200) 11.28%
Apr
May
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2024
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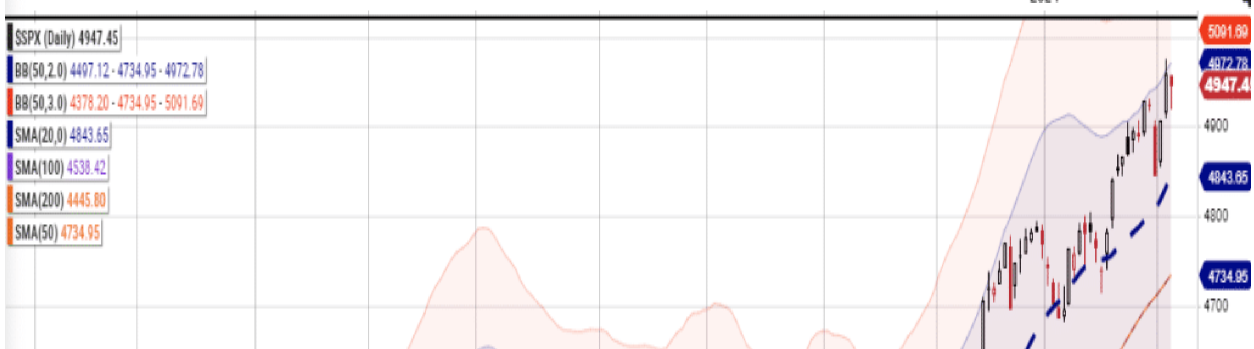
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SMA(20,0) 4843.65
SMA(100) 4538.42
SMA(200) 4445.80
SMA(50) 4734.95

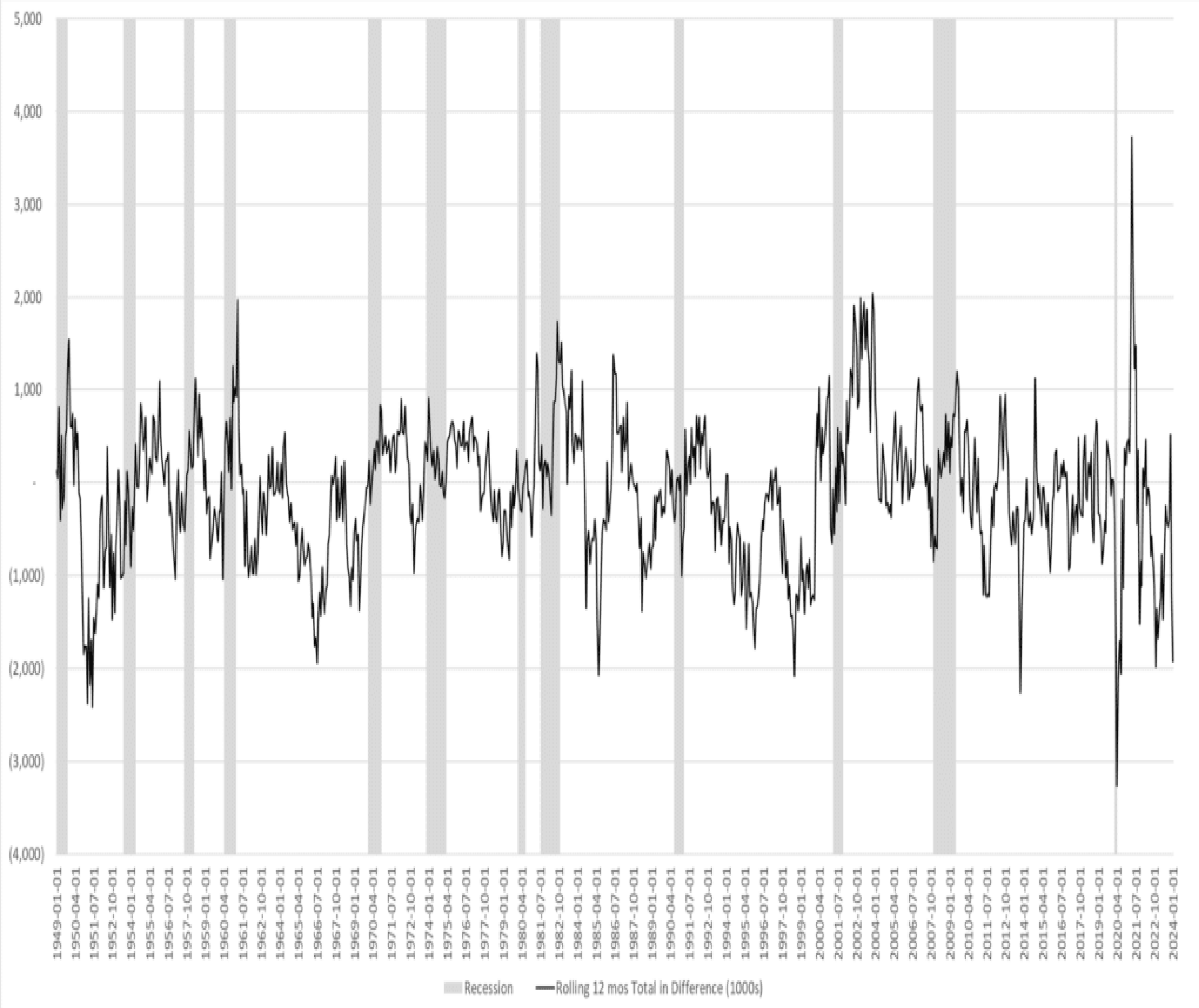
Earnings have continued to support the bullish momentum so far, but by the end of this week, a majority of those earnings will have been reported. Look for weakness in the latter half of February to increase equity exposures as needed.

More On The Jobs Divergence

[Monday?s Commentary] discussed the recent BLS jobs data and, in particular, pointed out the odd discrepancy between the two surveys used to calculate the report. To wit:

> *The biggest puzzle is the stark difference between the establishment and household surveys. The BLS establishment figure uses surveys of large companies to calculate the headline +353k number that is widely reported. The household survey gets its data from individuals. This data feeds the unemployment rate. The Household survey reported that the economy lost 31k jobs last month. The graph below shows the growing divergence between the two. In the previous two months, the household survey reported a loss of 714k jobs, while the establishment survey reported a gain of 686k.*

An inquisitive client of ours decided to expand on our findings. Therefore, as he highlights below, the 12-month cumulative difference between the two surveys is nearly 2 million jobs. Other than for a brief instance in early 2020, the current divergence is about as wide as it gets over the last 70 years. The second graph smoothes out the cumulative data over three years. As it shows, the establishment survey has reported 3.5 million more jobs than the household survey.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2016-07-01
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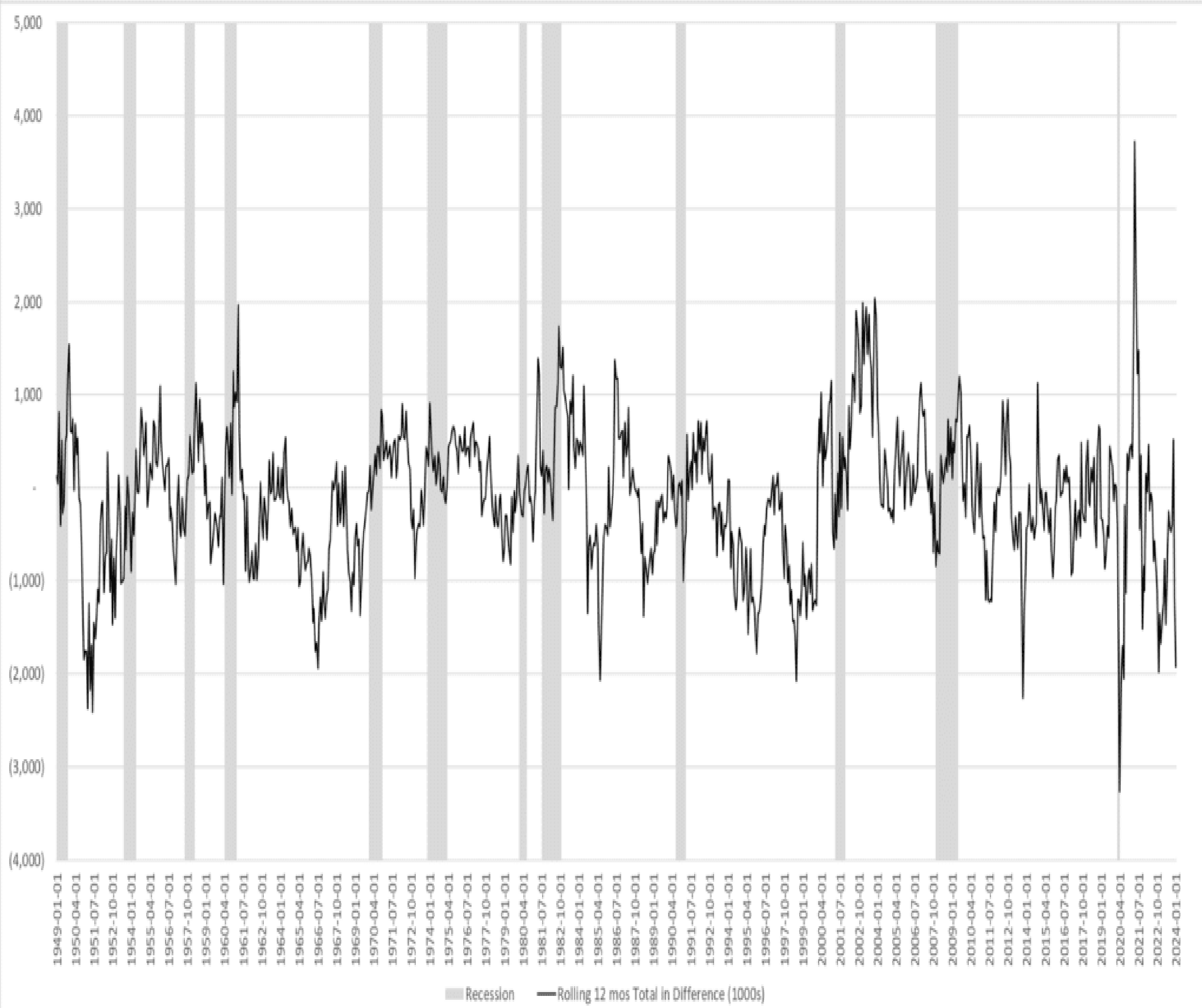
2021-07-01
2022-10-01
2024-01-01
Recession
Rolling 12 mos Total in Difference (1000s)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(4,000)
1949-01-01
1950-04-01
1951-07-01
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1960-04-01
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2022-10-01
2024-01-01
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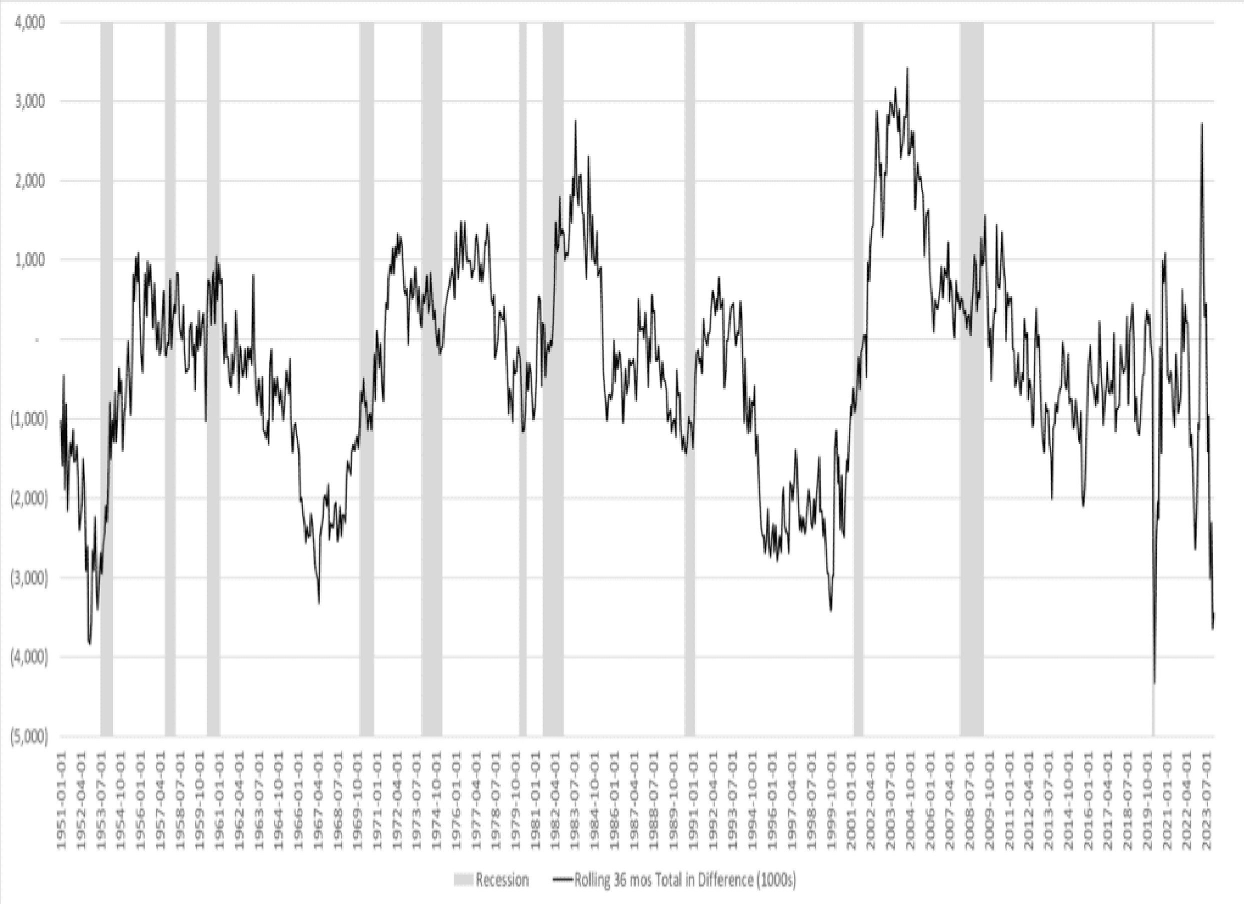
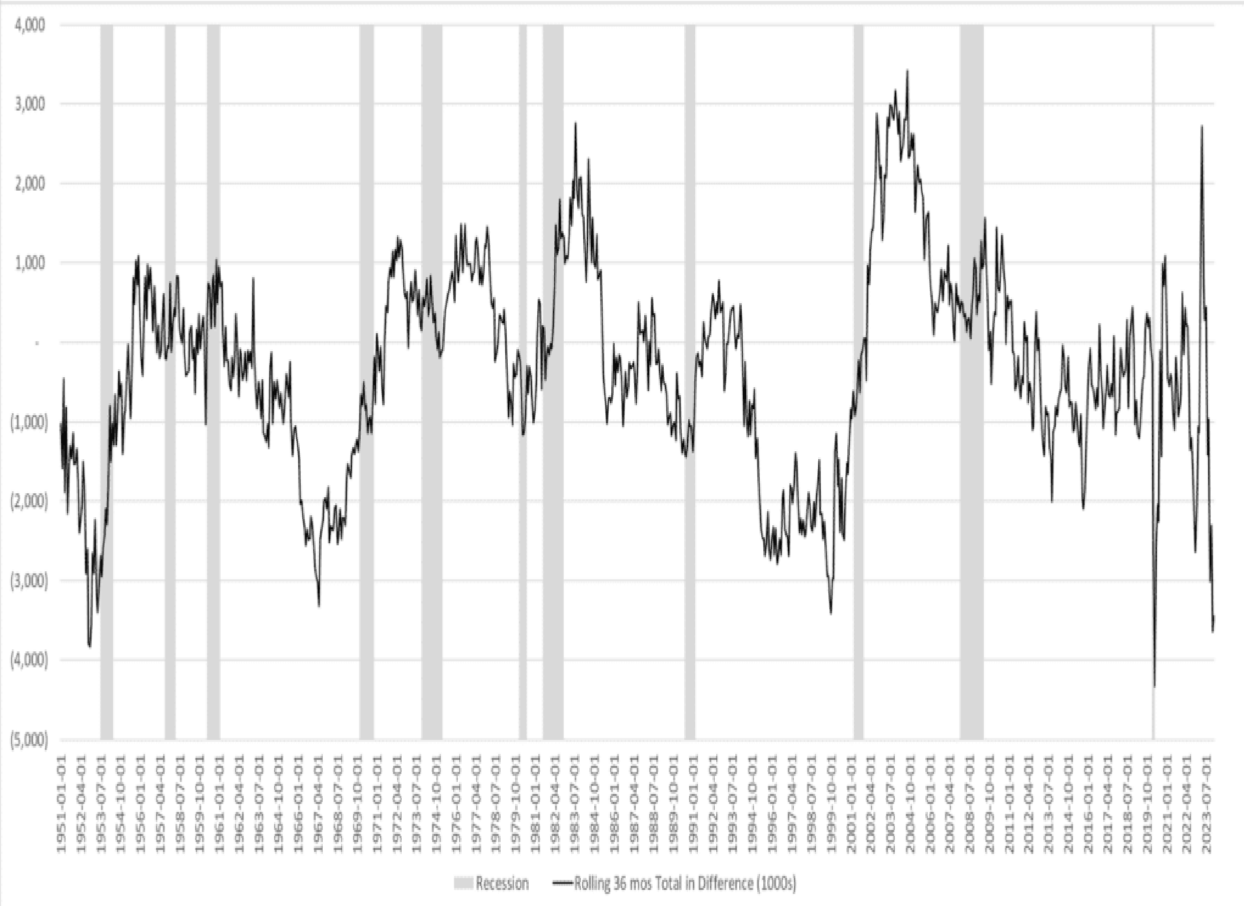




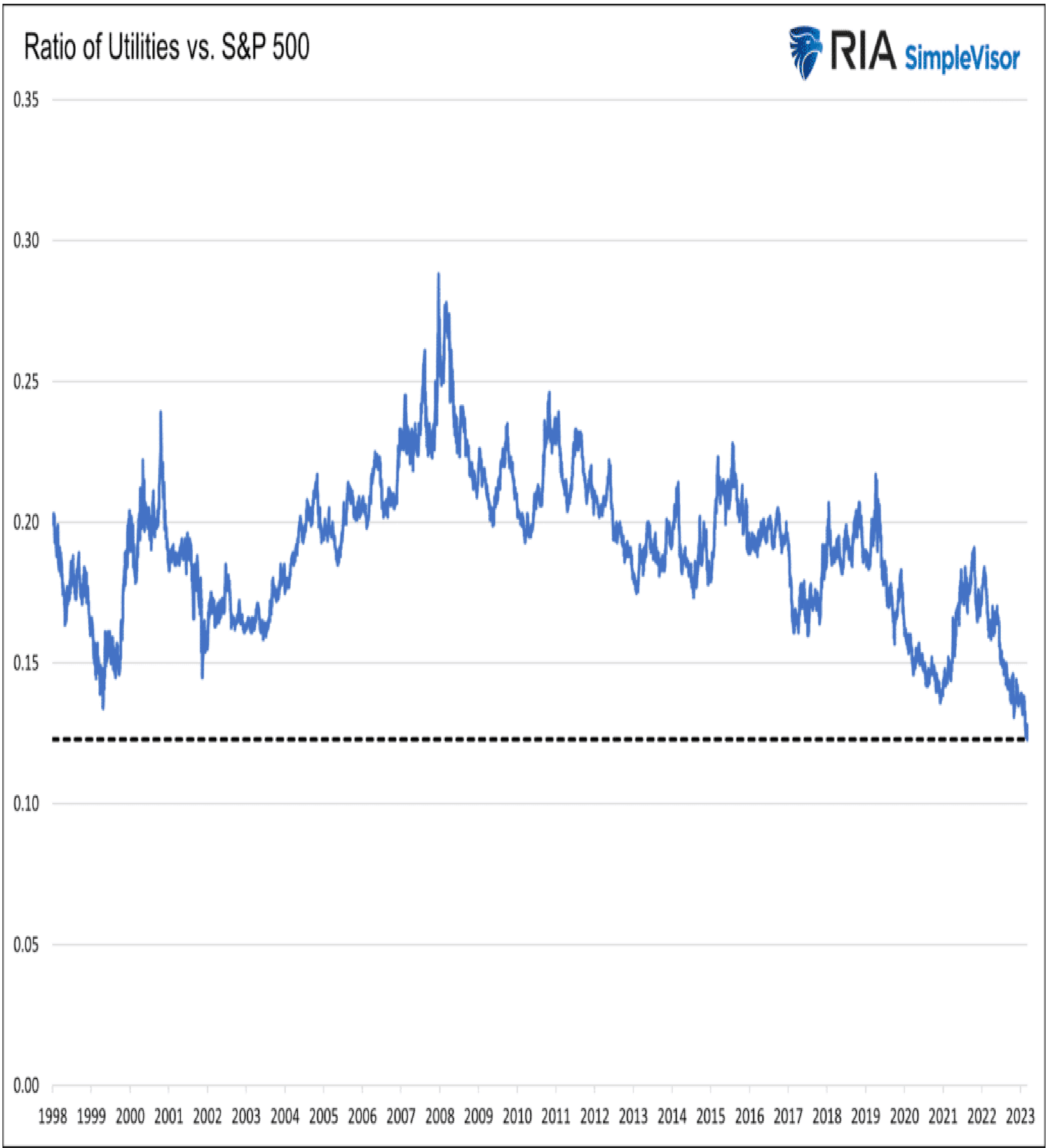
He correctly sums up his graphs as follows:

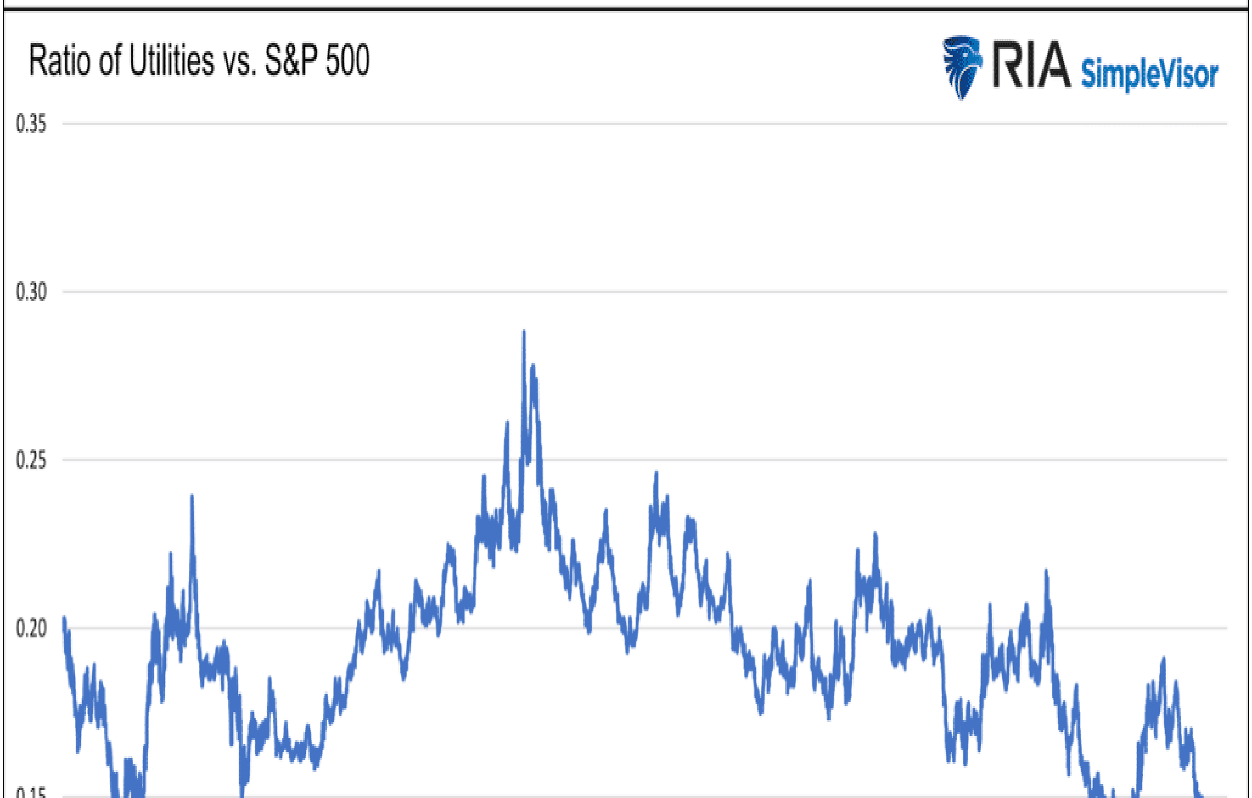
> *However, as the graphs indicate, usually this difference ?snaps back? over time.&#2013266080; &#2013266080;So, if history serves as any precursor my guess is*

not only will the BLS be doing their usual revisions to jobs data over time, but the monthly change in establishment Survey will be more in line w the household Survey over time.&#2013266080;&#2013266080;

Utilities Are Dirt Cheap

The price of the Utility sector (XLU) is now trading at a 25-year low in relation to the market (S&P) 500. Since peaking in 2008, the ratio of utilities to the S&P 500 has set a series of lower highs and lower lows. Based on the graph, it appears that utilities may be due for a bounce versus the market. Lower interest rates and or a weaker stock market could lead to such an event. However, we caution you that the trend is clearly not your friend.


Ratio of Utilities vs. S&P 500
RIA SimpleVisor
0.35
0.30
0.25
0.20
0.15
0.10
0.05
0.00
1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022 2023


Ratio of Utilities vs. S&P 500
RIA SimpleVisor
0.35
0.30
0.25
0.20

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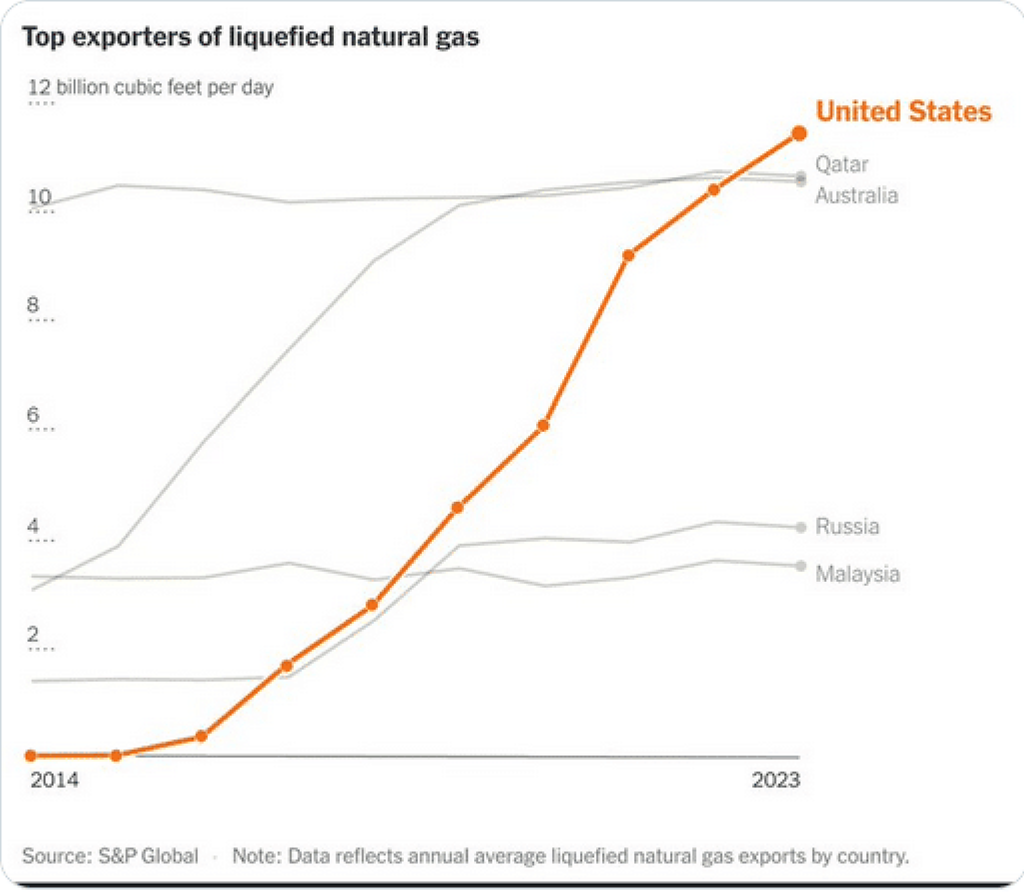
Go America. We're the largest exporter of natural gas on Earth.



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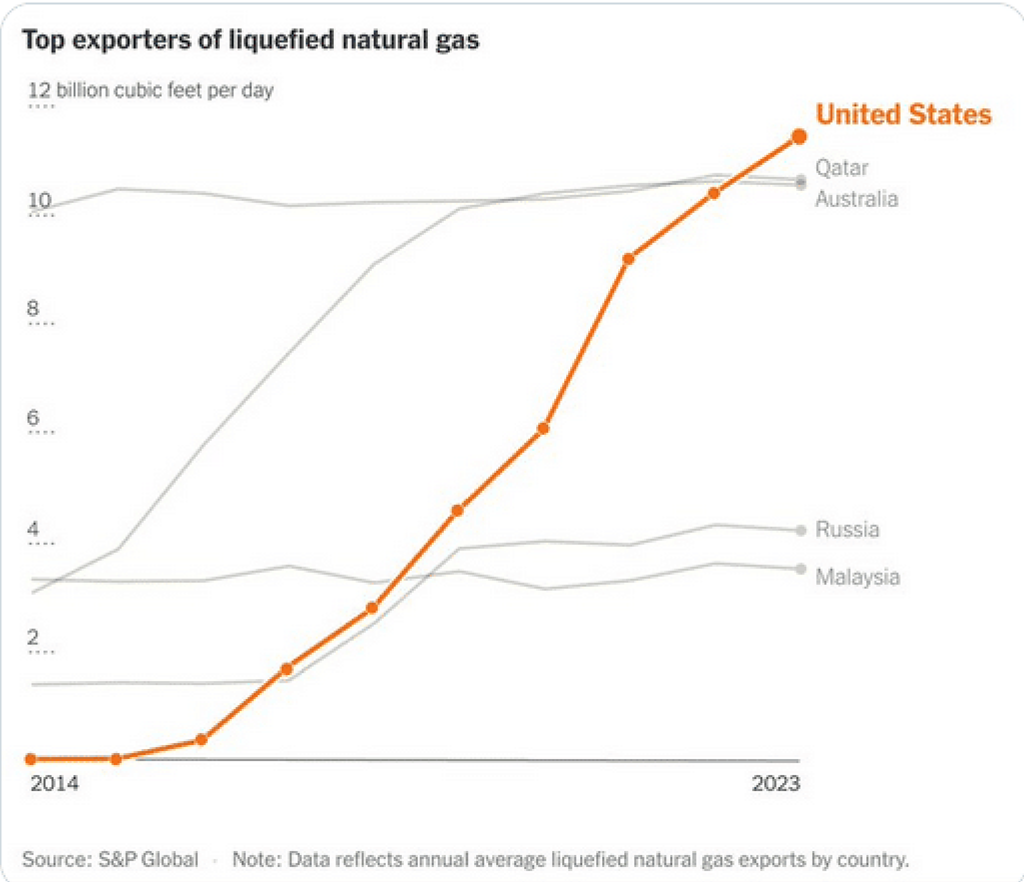

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2024/02/06

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