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Mortgage, interest rate woes weaken bank stocks

Return on investment suffers as earnings feel economic pinch

By CLAUDE SOLNIK

Quick: Name the nation's top banking towns. New York City? L.A.? Boston? Chicago? No, nope, nuh-uh, negative.

Try Mobettie, Texas. How about Cheyenne, Wyo.? Don't forget Trenton, Tenn., and of course Wetherford, Okla.

Unless you're a resident of Mobettie, you've probably never heard of it. But banks in these areas finished toward the top of the Independent Banker's 2006 list of the top 20 performers. Not a single Long Island institution made the banking trade publication's cut, which is based on return on investment.

It turns out Long Island-based community banking stocks (and community bank stocks nationwide) are lagging, as the sector faces challenges from mortgage woes, low interest rates and a continuing real estate market slowdown.

For the week ended June 4, four of the five worst-performing stocks on the Long Island Index (Long Island's 40 biggest public companies) were financial institutions. American Home Mortgage was trading at $22.01, down 37.3 percent for the year, followed by Suffolk Bancorp ($31.40, down 17.7 percent) and Smithtown Bancorp ($23.41, down 13.3 percent). Astoria Financial ($26.86, down 11 percent) rounded out was has been, to say the least, a bad year for many Island-based community banking stocks.

David Danielson, president of Vienna, Va.-based bank consulting firm Danielson Capital, said banks have faced an interest rate squeeze that has hurt earnings.

"It's a tougher banking environment," Danielson said. "All banks are having trouble increasing their net income quarter to quarter. A lot of the stock prices had got ahead of themselves and are correcting themselves to where they have been historically."

And some small banks have been caught up in overall sector concerns, he added, even if they've performed well. "Anything that's mortgage related [has been hurt]," Danielson said. "Some banks go down that probably shouldn't have gone down."

Bigger banks overall have done better, since they rely less on interest income. Savings and loan institutions, Danielson noted, often face the most difficulty, but overall, the banking industry isn't faring badly. All told, banks earned $145.7 billion in 2006, up $11.8 billion from 2005, according to Independent Banker.

But banks with under $100 million in assets earned $1.7 billion in 2006, down 10 percent from 2005. Bigger banks – with $100 million to $1 billion in assets – did better, earning $14.55 billion, up 1 percent form a year ago.

The banking industry's return on asset rate was flat at 1.28 percent, but return on equity slipped to 12.34 percent from 12.45 percent in 2005. Banks with fewer than $100 million in assets had a 0.93 ROA, down from 1 percent, while ROE fell to 7.1 percent from 8 percent a year earlier.

Banks with $100 million to $1 billion in assets had a 1.17 ROA and an 11.32 ROE – down from 1.24 and 12.09, respectively.

Banks heavily involved in mortgage lending took harder hits than those in commercial lending. The average mortgage lending rate on a 30-year fixed-rate mortgage was 6.52 percent for the week ended May 29, according to Calabasas, Calif.-based Informa Research Services.

Paul Merski, chief economist and director of tax policy for the Independent Community Bankers Association, publisher of Independent Banker, said he sees better things ahead for community banks. Low unemployment, good corporate earnings and a strong stock market should benefit community banks, he noted.

"The economy will remain resilient in 2007 and good for the community banking industry," Merski said.

How Low?

As of June 4, four of the Long Island Index's five worst-performing stocks were financial institutions.

COMPANY	JUNE 4 CLOSE	2007 PERCENT CHANGE
American Home Mortgage	$22.01	Down 37.3
Suffolk Bancorp.	$31.40	Down 17.7
Smithtown Bancorp.	$23.41	Down 13.3
Astoria Financial	$28.86	Down 11