

Profitable INVESTING Tips

Stock Market Investing Tips, Techniques, and Resources



Are Banks Ready to Break Out?

Hopes of deregulation are part of why financial stocks are up. And investors may be moving some money out of an overvalued tech sector. The bottom line is that **US bank stocks hit a post-crisis high** according to *The Financial Times*.

US financial stocks closed at the highest level in nearly 10 years on Tuesday as hopes for deregulation of banks grow and investors ditch technology stocks for the previously unloved banking sector.

Shares of some of the country's largest lenders, including Citigroup, Bank of America and JPMorgan, climbed more than 1 per cent on Tuesday, pushing the S&P 500 financial index to 419.54 – a level it last touched in December 2007 before the financial crisis had fully taken hold.

The gains came ahead of a move by the Office of the Comptroller of the Currency, which oversees national banks, to start the process of amending the Volcker rule, which bans banks from speculating with their own capital. On Wednesday, the OCC will formally seek public comment from banks and others on how the rule is working, people familiar with its plans told the Financial Times.

Banks passed the Federal Reserve stress test in June and since that time have outperformed the broader stock market. Interest rates are not going up all that fast which would normally put a damper on financial stocks but the promise of deregulation has raised these stocks. So, are bank stocks ready to break out?

Upside Potential

Both *Barron's* and *Investor Place* argue that banks have a lot of upside potential. Their arguments are based on the deregulation argument. Does that translate to higher **intrinsic stock value**? If you think that financial stocks will break out for a year or so you will plan on investing short term and if you believe that their return on equity invested will continue over the years due to the benefits of deregulation then you will be in for the long haul. But, why is there deregulation in the first place. Weren't there problems that nearly demolished the US and global economy? If congress and the president go ahead with deregulation will there be problems again down the road?

Why Are Banks Regulated?

The Federal Reserve Bank of St. Louis posts an article, **Why Are Banks Regulated?**

Banking regulation has existed in some form since the chartering of banks and its goals have evolved over time. Today, banking regulation serves four main purposes.

Financial Stability: *Instability in the financial system can have material ripple effects into other parts of the domestic and international financial sectors. Supervision that is focused on financial stability (often called macro-prudential supervision) looks at trends and analyzes the likelihood for financial contagion and the possible impacts across firms that pose systemic risks.*

Protection of the Federal Deposit Insurance Fund: *Since Jan. 1, 1934, the Federal Deposit Insurance Corp. has insured the deposits held in U.S. banks up to a defined amount (currently \$250,000 per depositor per bank). The federal government serves as a backstop to the insurance fund.*

In exchange for this insurance guarantee, banks pay an insurance premium and are also subject to safety and soundness examinations by state and/or federal regulators.

Consumer Protection: *Since the creation of the Federal Trade Commission in 1914, the federal government has had a formal obligation to protect consumers across industries. Since that time, numerous laws and regulations have been crafted by various agencies to protect bank customers and promote fair and equal access to credit.*

Competition: *A competitive banking system is a healthy banking system. Banking regulators actively monitor U.S. banking markets for competitiveness and can deny bank mergers that would negatively affect the availability and pricing of banking services.*

One only needs to remember the fraudulent lending practices that preceded the 2008 financial meltdown to hope that any deregulation is done carefully and oversight is maintained. Banks may indeed breakout to much higher levels if substantial deregulation occurs but investors will be wise to pay attention to the health of banks and the economy thereafter.

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