

ECONOMY

A Torrent
of Challenges

THINK STRATEGICALLY:

The Banking Sector Is at a Crossroads

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We have seen more transformative changes in the banking sector over these past two and a half years than most of us have witnessed throughout our entire careers. One of the most considerable changes has been the loan-to-deposit ratio in the U.S. and Puerto Rico rising to 60 percent. The other change has been the shift to 100 percent digital onboarding for accounts, credit cards and auto financing, among other products.

As the pandemic hit, it added more pressure for banks to transform digitally to lessen the need to go to brick and mortar branches. The historic shift was so high, that more than 40 percent of retail bank customers only use digital services today. Amid these shifts, a series of challenges are also affecting the banks, including rising interest rates, inflation, a slowing global economy and geopolitical risks.

Because of their involvement across all industries and many nations, banks have unique exposure through their lending operations; having that said, they are already feeling the impact, with most reporting a 50 percent or more reduction in investment banking fees, reductions in mortgage and auto loans and notable increases in loan loss reserves as we will discuss below.

U.S. vs. Puerto Rico Banks

Let us begin our analysis by examining the top nine U.S. and Puerto Rico bank holding companies, part of the Birling Capital U.S. Bank Index or the Puerto Rico Stock Index. We review how

each bank holding company's stock is performing from Jan. 1 to July 15 and compare it to the Dow Jones Industrial Average, S&P 500, Nasdaq composite, Birling Capital U.S. Bank Stock Index and Birling Puerto Rico Stock Index.

The returns of these five indices, ranked by performance, over the aforementioned period:

- Birling Puerto Rico Stock Index, -8.59 percent
- Dow Jones, -13.9 percent
- S&P 500, -18.95 percent
- Birling Capital U.S. Bank Index, -21.68 percent
- Nasdaq, -26.80 percent

Birling U.S. Bank Index vs. Birling Puerto Rico Stock Index, which one is ahead?

The Birling U.S. Bank Index has a -21.68 percent year-to-date (YTD) return, while the Birling Puerto Rico Stock Index yielded -8.59 percent YTD, and when pegged against the other indexes, the Birling U.S. Bank index beats the S&P 500 and Nasdaq.

How each bank holding company has performed individually and against these five indexes:

1. Firstbank Corp.(FBP), achieved a total return of -1.52 percent, beating the Dow, S&P, Nasdaq, Birling U.S. Bank Index, and Birling P.R. Stock Index handsomely. The stock price on July 15 closed at \$13.57 and had a price target of \$17.20. The company reports its 2022 second quarter (2Q22) earnings on July 22.

2. OFG Bancorp. (OFG), achieved a total return of -2.82 percent, beating the

Dow, S&P, Nasdaq, Birling U.S. Bank Index, and Birling P.R. Stock Index. The stock closed on July 15 at \$25.81, with a price target of \$35. The company reports its earnings on July 21.

3. Popular, Inc. (BPOP), achieved a total return of -6.81 percent, beating the Dow, S&P, Nasdaq, Birling U.S. Bank Index, and Birling P.R. Stock Index. The stock closed on July 15 at \$76.45, with a price target of \$107. The company reports its 2Q22 earnings on July 28.

4. Wells Fargo & Co (WFC), achieved a total return of -8.38 percent, beating the S&P, Nasdaq & Birling US Bank Index handsomely. The stock price on July 15 was \$43.96 and had a price target of \$62.55. The company reported 2Q22 earnings on July 15.

5. Citigroup Inc. (C) has a YTD return of -17.24 percent, lagging behind the Dow Jones, Puerto Rico Stock Index, but beating the S&P 500, U.S. Bank Index and Nasdaq. The stock price on July 15 was \$49.98 and had a price target of \$70.50. The company reported its 2Q22 earnings on July 15.

6. Morgan Stanley (MS) has a YTD return of -17.33 percent, behind the Dow Jones, U.S. Bank Index, Puerto

Rico Stock Index, the S&P, but beating the Nasdaq. The stock price on July 15 was \$78.05 and had a price target of \$95.45. The company reported its 2Q22 earnings on July 14.

7. Goldman Sachs Group (GS) has a YTD return of -19.25 percent, beating the Nasdaq and lagging behind the rest. The stock price on July 15 was \$293.87 and had a price target of \$395.50. The company was reporting its 2Q22 earnings on July 18.

8. Bank of America Corporation (BAC) has a YTD return of -27.51 percent, lagging behind the Birling U.S. Bank Index, Birling P.R. Stock Index, Dow Jones, S&P 500 and Nasdaq. The Stock price on July 15 was \$32.25, with a price target of \$47.45. The company was reporting its 2Q22 earnings on July 18.

9. JP Morgan Chase & Co. (JPM) has a YTD return of -28.67 percent, less than the Birling U.S. Bank Index, Birling Puerto Rico Stock Index, Dow Jones, S&P 500, and Nasdaq. The stock price on July 15 was \$112.95 and had a price target of \$137.60. The company reported 2Q22 earnings on July 14.

The three Puerto Rico banks that make up the Birling Puerto Rico Stock Index are beating their stateside counterparts and all the key indices. With all the Puerto Rico banks' earnings reports due from July 21 to July 28, we will have a better sense of their continued performance and outlook.

Four U.S. Banks Reported Earnings: 2 Missed and 2 Beat Expectations

JP Morgan Chase, Morgan Stanley, Wells Fargo and Citigroup have already reported their 2Q22 earnings, and the results were optimistic, given that some beat estimates; others missed them.

- JP Morgan Chase (JPM) reported revenue of \$30.7 billion, up 1 percent, missing estimates, and net income of \$8.6 billion, or down 28 percent and missing forecasts. Also, global investment banking fees were down 54 percent, and the bank stopped stock buybacks as it reacted to the Fed's stress test and the requirement to increase its capital to face an economic downturn.

- Morgan Stanley (MS) reported \$13.1 billion in revenue, or down 11 percent,

missing estimates, and a net income of nearly \$2.5 billion, down 29 percent. The bank saw a 55 percent drop in investment banking and 6 percent decrease in wealth management.

- Wells Fargo & Co. (WFC) reported \$17.02 billion in revenue, down 16 percent and missing estimates, for a net income of \$3.119 billion, which is down 48.36 percent, but beat estimates. Wells Fargo increased its provision for loan losses by \$580 million.

- Citigroup(C) reported revenue of \$19.6 billion, up 9.18 percent and beating estimates, and net income of \$4.5 billion, or down 27.41 percent. Citi increased its provision for loan losses by \$375 million.

These four banks collectively reported revenues of \$80.42 billion, net income of more than \$18.71 billion, and loan loss reserves of nearly \$2.16 billion.

Birling Puerto Rico Stock Index Is Beating all Indices

As you can see, the Birling Puerto Rico Stock Index, at -8.59 percent, continues to beat the Birling U.S. Bank Index, -21.68 percent, by a significant margin as well as the Dow Jones, S&P 500, and Nasdaq Composite. We think local stocks are worth looking into as part of a well-diversified portfolio of stocks, bonds and other securities in your long-term financial goals.

Week in Markets: U.S. Sales Rise, Bank Earnings and Wall Street Closes Week Down

The U.S. stock market, while up Friday, closed the week marginally down as the combination of four of the world's largest banks reported 2Q22 results, with two beating and two missing estimates. Also, unemployment claims rose 3.83 percent for the second consecutive week. On a positive note, the Core Producer Price Index fell for the fourth straight month to 8.24 percent, a decrease of 14.16 percent. Retail sales rose to 7.73 percent, and the closely watched University of Michigan Index of Consumer Sentiment rose to 51.1.

Francisco Rodríguez-Castro is president and CEO of Birling Capital LLC. Think Strategically© is a publication by Birling Capital LLC that summarizes recent geopolitical, economic, market and other developments. This report is intended for general information purposes only and does not represent investment, legal, regulatory, or tax advice. Recipients are cautioned to seek appropriate professional counsel regarding any of the matters discussed.

Weekly Market Close Comparison	7/15/22	7/8/22	Return	YTD
Dow Jones Industrial Average	31,288.26	31,338.15	-0.16%	-13.90%
Standard & Poor's 500	3,863.16	3,889.38	-0.67%	-18.95%
Nasdaq Composite	11,452.42	11,636.31	-1.58%	-26.80%
Birling Puerto Rico Stock Index	2,631.89	2,640.21	-0.32%	-8.59%
U.S. Treasury 10-Year Note	2.93%	3.09%	-5.18%	1.50%
U.S. Treasury 2-Year Note	3.13%	3.12%	0.32%	1.50%