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Flipping the field...sort of

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The Tennessee Titans defeated the Cleveland Browns on Oct. 16. It was the Titans' third victory of 2016, which equaled the number of victories recorded in 2015.

The Titans have been awful for several years. One of the reasons for what I think is a legitimate turnaround is not so much QB Marcus Mariota as a running game, which makes Mariota less of a piñata if he does not have to throw as much. Consistent production from running backs implies ball control for the offense and it increases the odds of a long run. If a long run (or pass) occurs when the offense has the ball near its goal line, it is called flipping the field — a single play that changes the character of the series and sometimes the game in which field position is swapped for the better.

Although it is early in the bank reporting season there has not been any field flipping as far as the industry is concerned. Yes, fixed income capital markets at JPMorgan Chase & Co., Citigroup Inc. and Bank of America Corp. were very good, but the business is volatile and a low-multiple earnings contributor, in my view.

More emblematic was the lack of what equity investors usually obsess over: growth. JPMorgan reported a 6% year-over-year reduction in quarterly earnings to $1.58 per share while year-to-date earnings declined 4% to $4.48 per share. Wells Fargo & Co. was similar with quarterly earnings down 2% YOY to $1.03 per share and YTD earnings down 3% to $3.03 per share. Citigroup posted lower quarterly and year-to-date earnings, too, on a YOY basis, while Bank of America posted higher results, partially as a result of cost-cutting efforts.

Large banks are not much of a growth proposition. Swings in profitability are usually attributed to a change in the economy from expansion to recession, and vice versa. The U.S. economy may have slowed this year, but it is not in recession. No surprise then that credit from a broad perspective appears to be fine such that I and many others might argue that profitability is overstated today by low credit costs.

Although it definitely does not count as flipping the field, I think the announcement by Opus Bank that it will post a loss in the third quarter as a result of charge-offs associated with eight credits bears watching for a number of regional banks as it relates to lending to technology companies. I doubt Opus is going to represent a one-off as it relates to technology lending. The sector had access to vast sums of capital provided by investors and lenders (including BDCs and credit funds) for a number of years.

Perhaps the peak of the mania — if that is what it was — coincided with the designation of some companies as "unicorns" based upon a valuation of at least $1 billion in the most recent fundraising round. Once investors began to more critically examine valuations and the sustainability of business models, investment capital flows began to slow and the ability of private equity investors to monetize their investments via IPOs and M&A became more difficult. Loss recognition for lenders should be expected to increase when capital flows slow; however, I think it will be a limited duration issue similar to what has transpired with energy lenders.

The one field-flipping scenario that banks may face before the next broad credit cycle or negative interest rate policy in the U.S. emerges is political rather than operational. If some of the political pundits are to be believed, Secretary Clinton will win the election and will govern with the Senate and House majorities flipping to the Democrats. The odds may be long for a running the table scenario for Democrats (and vice versa for Republicans), but it probably is not a scenario relished by many bankers.

Assuming no changes in committee assignments, Sen. Elizabeth Warren, D-Mass., will have greater power to influence policy as a member of the Banking, Housing and Urban Affairs Committee and its various subcommittees. Rep. Maxine Waters, D-Calif., would become the ranking member of the majority party of the House Committee on Financial Services.

I am not on thin ice in suggesting both would be tough congressional overlords. Warren in particular should not be expected to take a victory lap. During the month of October alone, she made headlines by opining that ex-Wells Fargo CEO John Stumpf should be criminally investigated (she is a lawyer) and that President Obama should ax Mary Jo White as Chair of the Securities and Exchange Commission.

Perhaps I exaggerate somewhat, but the Senator may be one of the most consequential figures for the banking industry since President Roosevelt, given her importance to the establishment of the Consumer Financial Protection Bureau and who knows what may follow. Maybe it would not really amount to flipping the field, but under such a scenario the banks could become bigger piñatas.

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