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Banks' Q3 earnings show they're preparing for a tough economic climate

Article

The news: The biggest banks in the US released their Q3 earnings over the past few days. Most of the results mirrored Q2 results, but with a less-upbeat outlook for the rest of this year and 2023. Revenue and earnings were up in most cases, beating analysts' expectations. But the looming recession looks closer than ever, and banks are preparing.

Here are the common themes we saw:

Theme 1: Profits mostly tumbled again

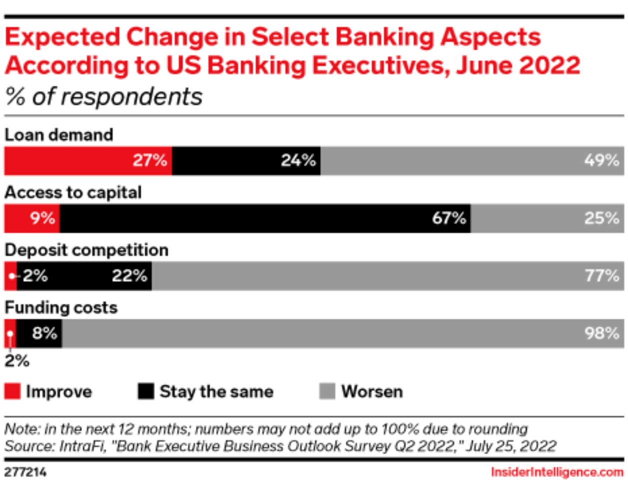
Similar to Q2, US banks saw their profits fall year-over-year in the most recent quarter.

- **Wells Fargo** saw a 31% profit decline.
- **Morgan Stanley's** profit decreased by 30%.
- **Citigroup's** profit fell by 25%.
- **JPMorgan** fared slightly better with a 17% decrease.
- **Bank of America** saw the smallest profit decline of 8%.

Theme 2: Loan delinquency is low, but loan loss provisions are high

Nearly all banks stated their falling profits were a result of setting aside large sums of money to cover potential losses from loan defaults. But many banks said that the low employment rates have allowed customers and businesses to continue to repay their loans, and currently loan delinquencies are low. The move to set aside credit provisions is fueled by the economic downturn trending toward a recession.

- JPMorgan added $808 million to its loan provisions.
- Wells Fargo set aside $784 million.
- Bank of America reserved $378 million for credit losses.
- Citigroup set aside $370 million.

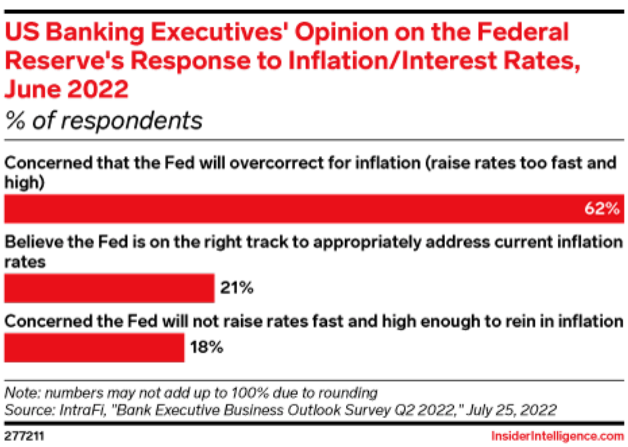


Theme 3: Personal banking boosted revenues, but investment banking took a beating

Increasing interest rates proved to be beneficial for US banks, as interest income drove revenue in Q3. But the downturn in M&A activity and debt and equity financing led to slumping investment banking performance.

- Citigroup saw a 10% increase in personal banking revenue YoY, a clear result of rising interest rates. But its investment banking arm reported a 60% decrease in revenue YoY.
- JPMorgan also saw a 10% revenue increase as it expanded its loan book in the quarter.
- Morgan Stanley took a rough hit to its investment management (revenue down 20%) and investment banking (revenue down 55%) businesses, citing a slow quarter for IPOs and minimal debt and equity issuances.
- Bank of America saw its loan book grow by 12% YoY, along with a 12% rise in personal banking revenue driven by increased interest rates. The bank also cited strong returns from fixed income trading activities.

It's noteworthy also that Wells Fargo, which is the biggest mortgage lender of the banks, reported a 52% decrease in mortgage lending revenue. This was due to rising home interest rates and a cooling housing market.



What's ahead? Bank CEOs touted the robustness of their banks after posting their Q2 earnings, stating their capital reserves were strong and that they were ready to weather the economic downturn. The banks are still in a relatively secure position, but CEOs are now striking a different tone as Q3 earnings are released.

- **85% of global bank heads are predicting a recession in the US** some time in the next 12 months, per KPMG.
- Q3 releases echoed this sentiment, with many CEOs citing the Ukraine war, inflation, and supply chain issues as major factors influencing the economy's health over the next few months.
- **According to KPMG, 49% of banks are planning for layoffs in the next six months** in response to growing pressure.

Earnings elsewhere: **Goldman Sachs** will be the final major bank to report its earnings, and we expect it to touch on similar themes. In the UK, banks are also facing grim economic pressures as rising inflation fuels a cost of living crisis, and a major energy crisis stemming from the war in Ukraine. Keep an eye out for coverage on UK bank earnings as they are released.

- **HSBC:** October 25
- **Barclays:** October 26
- **Lloyds Bank:** October 27
- **NatWest:** October 28

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