Global Banks Entering Bear Market Are Red Flag for US

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Shares of 16 Systemically Important Financial Institutions (SIFIs) are now in bear market territory, down by 20% or more from their recent highs in dollar terms, the Financial Times reports. This is sparking alarm in some quarters. "If these banks are supposed to be systemically important then policymakers ought to be watching them to see what is happening," says Ian Hartnett, chief investment strategist at London-based Absolute Strategy Research, as quoted by the FT. Taking this drop in bank share prices as an indicator of financial stress, Hartnett issued his first "Black Swan" alert since 2009.

Hartnett notes that many of these global banks have expanded their loan portfolios through borrowing, rather than by an increased intake of deposits. He adds that much of this borrowing has been denominated in U.S. dollars, with the result that these banks get squeezed when U.S. interest rates and the value of the U.S. dollar are rising, as they are now.

While none of the six largest U.S. banks by assets are among those 16, their share prices nonetheless are down significantly from their 52-week highs, following the global trend.

After getting big one-time boosts from tax cuts, the earnings of JPMorgan Chase, Bank of America and Citigroup U.S. are projected to experience significantly slower growth going forward. Additionally, their valuations on the basis of price to tangible book are the highest since 2010. (For more, see also: Why Big Bank Stocks Face More Steep Declines.)

Meanwhile, Morgan Stanley faces a similarly gloomy outlook, for the same reasons: decelerating earnings growth and a price to tangible book ratio that is the most expensive since 2012. (For more, see also: Morgan Stanley Stock May Fall 9% as Profits Sputter.)

It's much the same story for Goldman Sachs as well. (For more, see also: Goldman Sachs' Stock May Drop 9%.)

The Financial Stability Board (FSB), an international organization based in Basel, Switzerland, classifies 39 global banks as Systemically Important Financial Institutions (SIFIs), per the FT.

Among the 16 whose stock prices are down by 20% or more from their highs in U.S. dollar terms, several trade on U.S. markets, including these six:

The FSB fosters coordination among "national financial authorities and international standard-setting bodies" to promote a sound global financial system, per the FSB website. While there is some overlap, the U.S. Federal Reserve System has its own list of large banks that it considers to be systemically important and subject to the highest level of regulatory scrutiny under its annual Comprehensive Capital Analysis and Review (CCAR) process, often called the "bank stress test" process.

'Heading Down'

"The good news does not last forever," warns Bert Ely, an adjunct scholar at the Cato Institute and a consultant on financial institutions and monetary policy, also as quoted by the FT. Reacting to JPMorgan Chase & Co. CEO Jamie Dimon's remark that he sees "no real potholes" in the banking outlook, Ely reacted, “Those kind of comments are usually just before things start heading down.”