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Advice to take to the bank: 'Don't panic'

By MIKE MEYERS, Star Tribune
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In Pasadena, Calif., befuddled depositors at IndyMac Bank stood in line for hours this week to pull their money out of the vaults of the failed lender. Chances are, such bank runs will remain rare, bank experts say. And for most depositors -- those with less than $100,000 at any single federally insured bank -- their money is secure.

So far this year, **only five of the nation's 7,200 banks have failed**, ranging from California-based giant IndyMac to a small-town stalwart in Staples, Minn., First Integrity Bank, which was shuttered in May.

To match the 1989 peak in federal financial institution closings, 529 more banks would have to fail by the end of this year -- a prospect bank analysts say is so unlikely as to be ludicrous.

"I don't know if it's the Internet or the 24-hour news cycle, but I think if you asked most people out there how many banks have failed, their answer would be a lot greater [than five]," said Jon Arfstrom, bank analyst at the Minneapolis office of RBC Capital Management.

Longtime bank consultant Bert Ely, in Alexandria, Va., said the U.S. economy has many troubles, but bank failures are not among them. "Don't panic," Ely said. "There's incredible anxiety out there, far more than is justified."

Still, these are worrisome times for bankers and their customers. The housing crash has forced banks to write off billions in real-estate-related loans. And this week, U.S. Bancorp and Wells Fargo & Co., the two largest lenders in the state, reported double-digit declines in earnings. But those results were better than expected, sparking a rally in bank stocks -- a rally some see as a sign investors are reassessing the risks to the banking system.

Indeed, Federal Deposit Insurance Corp. (FDIC) records indicate that a relative handful of Minnesota banks have problems tied to construction loans gone bad -- a central problem that led to savings-and-loan failures in the late 1980s and early 1990s. "A lot of the problems aren't on bank balance sheets," Arfstrom noted.

Bundling helped small banks

Bundling home loans into securities sold to investments has hit some Wall Street banks and investment funds hard. But, in a fact that's sometimes overlooked, the process freed smaller banks from holding home loans now in trouble.

"I don't think it's a horrific, cataclysmic problem," said Jim Paulsen, chief investment strategist at Wells Capital Management, an arm of Wells Fargo. Nevertheless, bearers of gloom still aren't hard to find.

An upturn for the bank's financial fortunes will be linked to the course of the economy, said David Beim, professor of finance and economist at Columbia University's business school.

"For a long time, I've thought we are in for a much, much worse recession than people are thinking," he said. One reason for pessimism: Consumer debt as a share of household income is climbing as the value of a consumer's biggest asset -- a home -- falls. That's going to make banks less likely to lend and consumers less inclined to spend, in Beim's view.

"I anticipate a big recession, and I also anticipate a lot of banking problems," he said. Optimists and pessimists can find facts for their case in bank statistics.

After the costly process of foreclosing on property, U.S. financial institutions were stuck owning $16.6 billion in real estate at the end of the first quarter -- double the amount in the same period of 2007 and triple the total in the first quarter of 2006.

At the end of March, lenders backed by federal deposit insurance owned $1.3 trillion in mortgage-backed securities -- 53 percent more than at the start of the decade, even after adjusting for inflation. The share of bank loans tied to real estate has grown considerably in recent years, according to a Star Tribune analysis of FDIC records.

In the first quarter of this year, the latest figures available, residential and commercial real estate accounted for 46 percent of all loans outstanding at U.S. banks and savings-and-loan institutions. In 1984, the first year the FDIC kept comparable statistics, such loans accounted for 34 percent of all loans

To Andrew Witton, chairman of the finance department at the University of Minnesota's Carlson School of Management, the next turn in the banking cycle will have less to do with the banks themselves than with the fate of the housing market.

"I think there's more risk than the last two downturns," Witton said. "The housing market is in such trouble."