



Equity Strategy

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March 3, 2013

*Financial Stocks Weekly: Energy Independence Could Be a Boon for Banks*

**Summary--**The rapid move toward energy independence in the U.S. is being driving by new oil and gas drilling and extraction technologies that are opening up new fields throughout the country. For banks in these regions this can mean increased deposits, lending and wealth management income. Since 2009, the states that have seen the greatest increase in the number of oil and gas rigs, as discussed in this note, are Texas, North Dakota, Oklahoma, Pennsylvania, New Mexico and California. The expansion of natural gas drilling slowed in 2012 due to low prices. However, as those prices have rebounded we expect that activity to pick up aiding the regional economies. The new technologies are more expensive than historical approaches and will likely be accommodated with environmental mitigation activities that will add to overall economic growth.

**Key Points--**

- We reviewed the regional banks located in where their expansion of energy activity in four regions: Texas and Oklahoma, the Marcellus Shale in the Northeast, North Dakota and Montana, and the southern San Joaquin Valley in California. Banks in those regions that could benefit from expanded economic activity include: BOKF, CFR, FFIN and TCBI in the Texas/Oklahoma region; CBU, FCF, FISI, FNB, NPBC, NWBI, PEBO and STBA in the Marcellus Shale region; BSRR and TCBK in California; and FIBK and GCBI in North Dakota/Montana.
- **The Week Ahead:** The highlight of the week for financial stocks will come Thursday afternoon when the Federal Reserve releases its stress test results for the largest banks. We expect all of the publicly traded banks to pass the test. Further, these test results should give some indication of the capital deployment that will be allowed by large banks; however the exact capital plans will not be released for another week. In addition, we expect most financial firms will have filed their 10Ks by early in the week and a competitor has a broad-based financial services conference on Tuesday and Wednesday. The events for the coming week are included in Exhibit 10 of this report. The complete KBW Catalyst Calendar can be accessed from the home page of the KBW research library.
- **The Week Behind:** Financial stocks lagged the overall market last week, down 0.6% compared to the market increase of 0.2%. The lag was primarily due to the decline in the 10-year bond yield and weak stock price performance by large banks and life insurance companies. Earnings estimate revisions continued the positive trend that has been evidence since earnings were announced, with 42 upward revisions compared to 23 downward revisions. The Universal Banks sector drove upward revisions.

## Financial Stocks Weekly: Energy Independence Could Be a Boon for Banks

Increased oil and gas production coupled with stable energy demand is narrowing the gap between supply and demand for energy in the U.S. and has prompted numerous forecasts of U.S. energy independence in the next 10 to 20 years. The growth in supply is driven by new technologies and capabilities, including fracking, that have opened up new oil and gas fields throughout many regions of the country. Exhibit 1 presents the expansion of oil and gas rigs by state since 2009. As shown, the growth has been greatest in Texas, North Dakota, Oklahoma, Pennsylvania, New Mexico and California.

**Exhibit 1: Greatest Increases in Average Rig Counts by State Since 2009**

State	Rig Count 2012	Rig Count 2009	Change #	Change %	Unemployment Rate 2012
TEXAS	899	432	467	108%	6.1%
NORTH DAKOTA	188	50	138	276%	3.2%
OKLAHOMA	196	94	102	109%	5.1%
PENNSYLVANIA	84	42	42	100%	7.9%
NEW MEXICO	84	44	40	91%	6.4%
CALIFORNIA	44	23	21	91%	9.8%
UTAH	37	18	19	106%	5.2%
MONTANA	20	3	17	567%	5.7%
COLORADO	65	50	15	30%	7.6%
OHIO	18	8	10	125%	6.7%
KANSAS	30	20	10	50%	5.4%
WYOMING	47	40	7	18%	4.9%
WEST VIRGINIA	26	22	4	18%	7.5%
MICHIGAN	2	0	2	nm	8.9%
SOUTH DAKOTA	1	0	1	nm	4.4%
NEBRASKA	1	0	1	nm	3.7%
MISSISSIPPI	11	10	1	10%	8.6%
FLORIDA	1	0	1	nm	8.0%
ALABAMA	5	4	1	25%	7.1%
ILLINOIS	1	1	0	0%	8.7%
WASHINGTON	0	1	-1	-100%	7.6%
INDIANA	1	2	-1	-50%	8.2%
HAWAII	0	1	-1	-100%	5.2%
ALASKA	7	8	-1	-13%	6.6%
TENNESSEE	0	2	-2	-100%	7.6%
NEW YORK	0	2	-2	-100%	8.2%
NEVADA	1	3	-2	-67%	10.2%
VIRGINIA	1	4	-3	-75%	5.5%
KENTUCKY	3	10	-7	-70%	8.1%
ARKANSAS	21	44	-23	-52%	7.1%
LOUISIANA	124	150	-26	-17%	5.5%
<b>UNITED STATES</b>	<b>1,919</b>	<b>1,086</b>	<b>833</b>	<b>77%</b>	<b>7.8%</b>

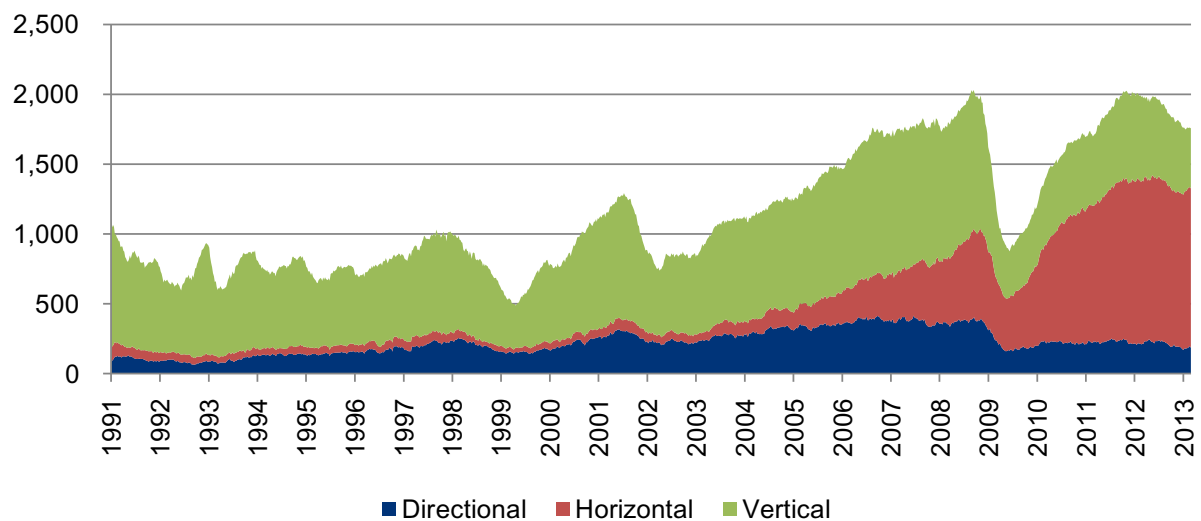
Note: Unemployment data as of 12/31/2012. Rig counts represent the annual averages by state as measured by the Baker Hughes census of the drilling rigs actively exploring for or developing oil or natural gas in the United States.

Source: Baker Hughes, Bureau of Labor Statistics, and KBW Research.

Banks located in the regions where this activity is located can benefit in numerous ways. First, local residents often get up-front one-time payments for the use of their land, boosting deposits and wealth management services. Next, as exploration and drilling increases, local businesses, including hospitality, expand. In addition, there is often significant water used in the drilling process, expanding local supply and hauling businesses. Finally, local residents receive royalty payments for the extracted oil and gas. In the future, local environmental mitigation firms may also find increased business activity. KBW analysts have written on these potential benefits to banks in the Marcellus shale regions. For more information, please see the note published 5/17/2011, titled, [Drilling Down on the Marcellus Shale: Recapping Our Trip to Western PA](#) and the note published 9/15/2010, titled, [Pennsylvania's Marcellus Shale: Bank Stock Plays](#).

The new technologies bring more economic activity into the regions because they allow companies to drill wells that were previously considered uneconomical or inaccessible. The growth in the use of new technologies is illustrated in Exhibit 2, which shows the difference in the well types. As shown, most of the growth since 2009 has been in horizontal wells, which are more complex and expensive than vertical wells.

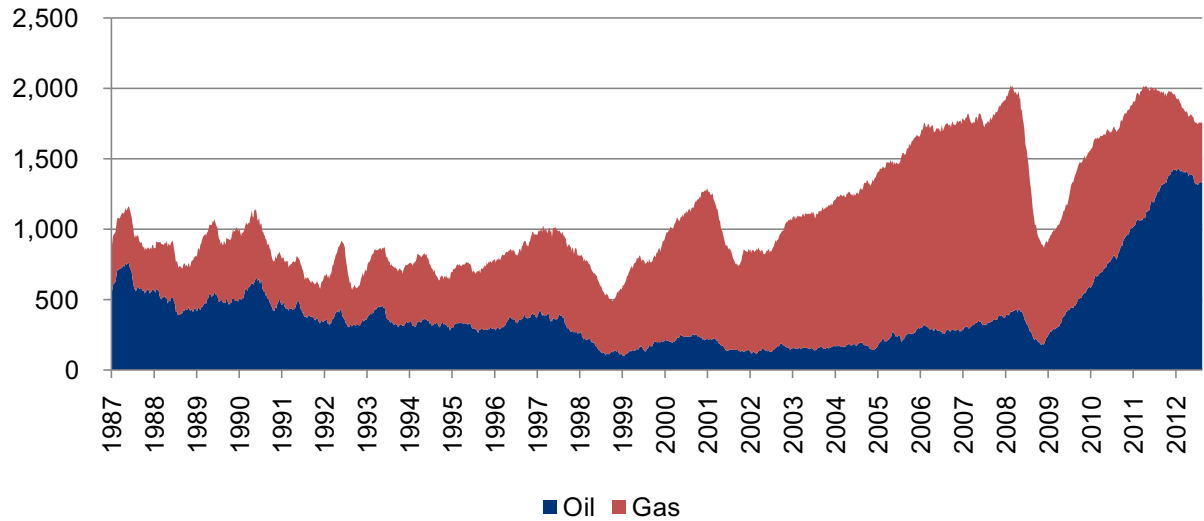
**Exhibit 2: Rig Count by Trajectory**



Source: Baker Hughes.

Although there has been an expansion in drilling since 2009, most of that expansion has been for oil rather than natural gas, as shown in Exhibit 3. This is due to the rise in oil prices relative to natural gas, which made drilling for oil more profitable than drilling for gas.

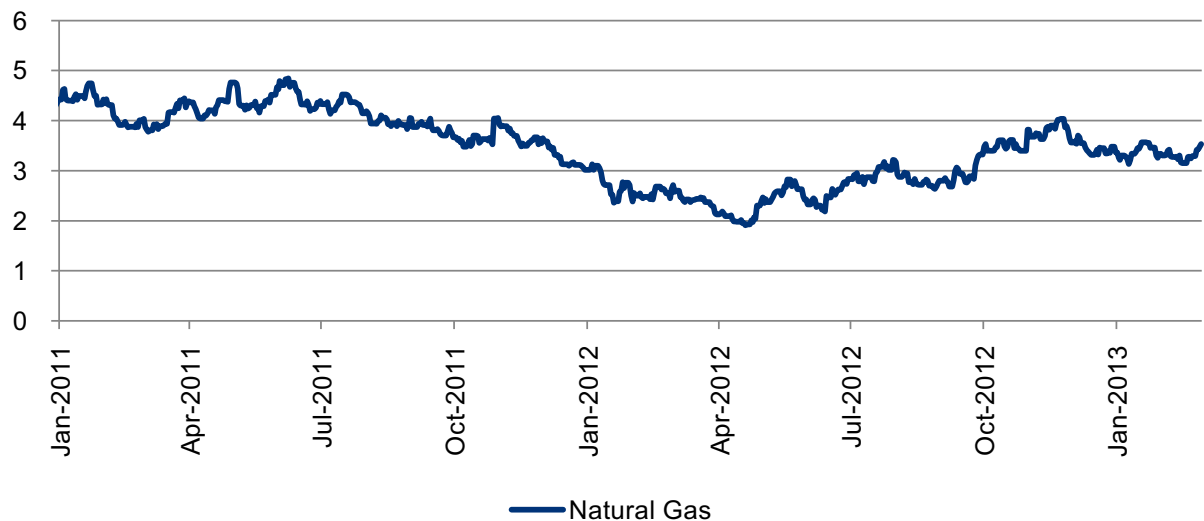
**Exhibit 3: Oil / Gas Split of Rig Count**



Source: Baker Hughes.

Moving forward, we expect greater expansion of natural gas production as those prices rise. And, natural gas prices are up, as shown in Exhibit 4. The expansion of regional economic activity should rise with the increase in gas prices and more drilling with new technologies.

**Exhibit 4: Natural Gas Prices Have Recovered from Lows**



Source: FactSet and KBW Research.

With economic activity expected to increase in the areas of expanded drilling, we polled KBW regional bank analysts as to which banks could benefit the most, and the results are presented in Exhibit 5. These are generally smaller banks with activity concentrated in the regions and sub-regions that could experience the most economic expansion. As shown, the banks identified include: BOKF, CFR, FFIN and TCBI in the Texas/Oklahoma region; CBU, FCF, FIS, FNB, NPBC, NWBI, PEBO and STBA in the Marcellus Shale region; BSRR and TCBK in California; and FIBK and GCBI in North Dakota/Montana.

**Exhibit 5: Banks Benefiting from Increased Drilling Activity**

Name	Ticker	Loan Growth		P/ TBV	Rating	Primary States of Operation
		2012/2011				
BOK Financial Corp.	BOKF	9.2%	1.57	MP		OK(86),TX(47),NM(22)
Sierra Bancorp	BSRR	16.2%	1.08	OP		CA(26)
Community Bank System Inc.	CBU	11.4%	2.10	MP		NY(160),PA(26)
Cullen/Frost Bankers Inc.	CFR	15.4%	2.06	UP		TX(129)
First Commonwealth Financial	FCF	4.0%	1.25	MP		PA(112)
First Financial Bankshares	FFIN	17.0%	2.92	MP		TX(57)
First Interstate BancSystem	FIBK	0.6%	1.38	MP		MT(38),SD(19),WY(19)
Financial Institutions Inc.	FISI	14.9%	1.49	MP		NY(54)
F.N.B. Corp.	FNB	18.7%	2.34	MP		PA(242),OH(15),WV(2)
Glacier Bancorp Inc.	GBCI	-2.0%	1.59	MP		MT(52),ID(25),WY(13)
National Penn Bancshares Inc.	NPBC	1.0%	1.61	MP		PA(125),MD(1)
Northwest Bancshares, Inc.	NWBI	2.5%	1.24	OP		PA(144),NY(19),MD(4)
Peoples Bancorp Inc.	PEBO	5.0%	1.50	OP		OH(26),WV(13),KY(4)
S&T Bancorp Inc.	STBA	6.9%	1.51	MP		PA(58)
Texas Capital Bancshares Inc.	TCBI	21.8%	2.11	MP		TX(13)
TriCo Bancshares	TCBK	0.9%	1.28	MP		CA(68)

Note: Primary states of operation are the three states with the most number of company offices. Loan Growth measures the year over year growth in loans held for investment. Pricing data as of 03/01/2013.

Source: SNL Financial, FactSet, and KBW Research.

## Financial Stock Earnings Revisions

Earnings estimate revisions continued the positive trend that has been evidence since earnings were announced, with 42 upward revisions compared to 23 downward revisions. The Universal Banks sector drove upward revisions.

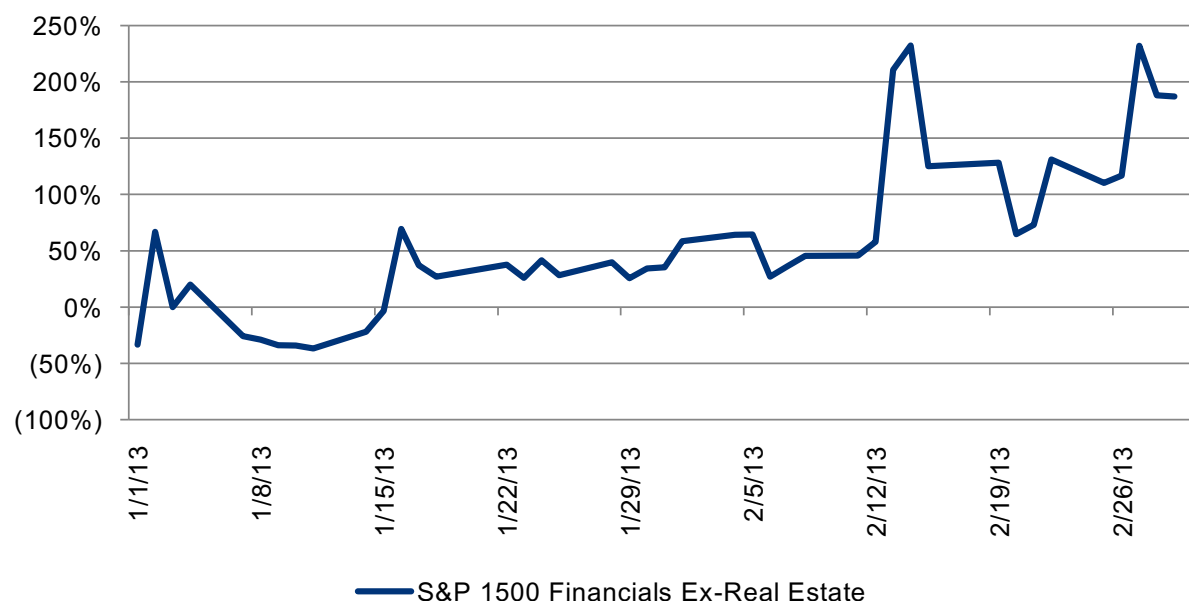
### Exhibit 6: Financials Earnings Estimate Revisions\*

Weekly EPS Estimate Revisions		
Sector	Upward	Downward
Universal Banks	14	2
Large-Regional Banks	2	3
SMID-Cap Banks	11	4
Capital Markets	3	3
Diversified Financials	1	1
P&C Insurance	8	4
Life Insurance	3	6
<b>S&amp;P 1500 Financials Ex-Real Estate</b>	<b>42</b>	<b>23</b>

\*Data as of 03/01/2013. Note: Upward and downward revisions measure the number of FY2 (next full unreported fiscal year) EPS estimate revisions to each constituent in the given sector.

Source: FactSet, Standard and Poor's, and KBW Research.

### Exhibit 7: Financials Earnings Revisions Year to Date\*



\*Data as of 03/01/2013.

Note: Measures the difference between the number of upward and downward EPS estimate revisions for companies within the S&P 1500 Financials as a percentage of downward EPS estimate revisions. Upward and downward EPS estimate revisions measure the number of FY2 (next full unreported fiscal year) EPS estimate revisions to each constituent in the S&P 1500 Financials during the previous week. Estimate Revisions for the S&P 1500 Financials exclude revisions for companies in the Real Estate sector.

Source: FactSet, Standard and Poor's, and KBW Research.



### Financial Stock Performance, Week Ending March 1, 2013

Financial stocks lagged the overall market last week, down 0.6% compared to the market increase of 0.2%. The lag was primarily due to the decline in the 10-year bond yield and weak stock price performance by large banks and life insurance companies.

### Exhibit 8: Week-to-Date and Year-to-Date Returns

Calculated Returns for the Week Ending:\*

KBW Model Portfolio	3/1/2013	S&P 1500 Financials	3/1/2013	Excess Return	3/1/2013
Universal Banks	(1.14%)	Universal Banks	(1.16%)	Universal Banks	0.02%
Large-Regional Banks	(0.34%)	Large-Regional Banks	(0.16%)	Large-Regional Banks	(0.17%)
SMID-Cap Banks	(0.61%)	SMID-Cap Banks	(0.54%)	SMID-Cap Banks	(0.06%)
Capital Markets	(0.62%)	Capital Markets	(0.47%)	Capital Markets	(0.15%)
Diversified Financials	0.10%	Diversified Financials	(0.08%)	Diversified Financials	0.19%
P&C Insurance	0.56%	P&C Insurance	(0.05%)	P&C Insurance	0.60%
Life Insurance	(0.80%)	Life Insurance	(0.83%)	Life Insurance	0.03%
<b>KBW Model Portfolio</b>	<b>(0.46%)</b>	<b>S&amp;P 1500 Financials</b>	<b>(0.60%)</b>	<b>Excess Return**</b>	<b>0.14%</b>
		<b>S&amp;P Composite 1500</b>	<b>0.16%</b>		

Calculated Returns for full year:

KBW Model Portfolio	2013	S&P 1500 Financials	2013	Excess Return	2013
Universal Banks	11.40%	Universal Banks	7.49%	Universal Banks	3.91%
Large-Regional Banks	(0.33%)	Large-Regional Banks	4.08%	Large-Regional Banks	(4.41%)
SMID-Cap Banks	5.02%	SMID-Cap Banks	7.71%	SMID-Cap Banks	(2.70%)
Capital Markets	14.06%	Capital Markets	11.77%	Capital Markets	2.29%
Diversified Financials	5.04%	Diversified Financials	9.04%	Diversified Financials	(4.00%)
P&C Insurance	12.60%	P&C Insurance	11.61%	P&C Insurance	0.98%
Life Insurance	4.94%	Life Insurance	6.44%	Life Insurance	(1.50%)
<b>KBW Model Portfolio</b>	<b>9.29%</b>	<b>S&amp;P 1500 Financials</b>	<b>8.43%</b>	<b>Excess Return**</b>	<b>0.87%</b>
		<b>S&amp;P Composite 1500</b>	<b>6.97%</b>		

\*Market-capitalization weighted returns as of 03/01/2013.

\*\* Excess return calculated arithmetically.

Note: Returns for the S&P 1500 Financials exclude the impact of companies in the Real Estate sector.

Source: Standard & Poor's, FactSet, and KBW Research.



### Exhibit 9: CDS Pricing

	Price 02/28/2013	-1 Day	-1 Week	Change vs.		
				-1 Month	-3 Months	-1 Year
BAC	124 bps	+2 bps	+1 bps	+13 bps	-25 bps	-134 bps
C	113 bps	-1 bps	-1 bps	+2 bps	-30 bps	-107 bps
JPM	81 bps	+1 bps	-0 bps	+0 bps	-22 bps	-29 bps
WFC	71 bps	-1 bps	-1 bps	+0 bps	-12 bps	-25 bps
GS	133 bps	+2 bps	-2 bps	-0 bps	-38 bps	-117 bps
MS	142 bps	-4 bps	-1 bps	+1 bps	-67 bps	-175 bps

Source: Bloomberg.

### Exhibit 10: Key Events in the Upcoming Week

KBW Catalyst Calendar				
March 2013				
Banks	Diversified Financials	Insurance	Macroeconomic	Europe
4 Euro-Area Finance Ministers Meet in Brussels (March)	5 EU-27 Finance Ministers Meet in Brussels (Mar) EU-27 Finance Ministers Meet in Brussels (March) Citi Financial Services Conf.	6 Germany to Sell Add'l EU4 Bln 5-Year Notes (3/6) Fed's Plosser Speak on Economic Outlook: Lancaster, PA Citi Financial Services Conf.	7 ECB Announces Interest Rates (Mar.) ECB Governing Council meeting in Frankfurt (3/7) Bank of England Monetary Policy Committee Decision Spain to Sell Bonds (3/7) ECB Deposit Facility Rate (Mar) Federal Reserve Releases Stress Test Results	8 Unemployment Rate (Feb)
Events expected week of March 4:				
Malta Holds Parliamentary Elections Italy Holds Regional Elections				

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Note: Dates listed in this report are subject to change. For access to our full catalyst calendar, please go to the home page of the KBW research library.

Source: Company reports, Bloomberg, and KBW Research.





## Companies Mentioned in This Report

- BOK Financial Corporation (BOKF: \$59.55, Market Perform)
- Sierra Bancorp (BSRR: \$12.94, Outperform)
- Community Bank System (CBU: \$28.84, Market Perform)
- Cullen/Frost Bankers Inc (CFR: \$60.40, Underperform)
- First Commonwealth Financial (FCF: \$7.35, Market Perform)
- First Financial Bankshares, Inc. (FFIN: \$45.02, Market Perform)
- First Interstate BancSystem, Inc. (FIBK: \$17.95, Market Perform)
- Financial Institutions, Inc (FISI: \$20.09, Market Perform)
- F. N. B. Corporation (FNB: \$11.49, Market Perform)
- Glacier Bancorp, Inc. (GBCI: \$17.47, Market Perform)
- National Penn Bancshares, Inc. (NPBC: \$9.91, Market Perform)
- Northwest Bancshares, Inc. (NWBI: \$12.55, Outperform)
- Peoples Bancorp Inc. (PEBO: \$21.72, Outperform)
- S&T Bancorp Inc (STBA: \$18.11, Market Perform)
- Texas Capital Bancshares, Inc. (TCBI: \$42.38, Market Perform)
- TriCo Bancshares (TCBK: \$17.01, Market Perform)

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Rating	Count	Percent	*IB Serv./Past 12 Mos.	
			Count	Percent
Outperform [BUY]	168	29.73	73	43.45
Market Perform [HOLD]	297	52.57	87	29.29
Underperform [SELL]	50	8.85	11	22.00



<b>Restricted [RES]</b>	<b>0</b>	<b>0.00</b>	<b>0</b>	<b>0.00</b>
<b>Suspended [SP]</b>	<b>50</b>	<b>8.85</b>	<b>9</b>	<b>18.00</b>
<b>Covered -Not Rated [CNR]</b>	<b>2</b>	<b>0.35</b>	<b>2</b>	<b>100.00</b>

\*KBW maintains separate research departments; however, the above chart, "Distribution of Ratings/IB Services," reflects combined information related to the distribution of research ratings and the receipt of investment banking fees globally.

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