

Cash Flow and Carey



Robert Carey, CFA
Chief Market Strategist



Peter Leonteos
Market Strategist

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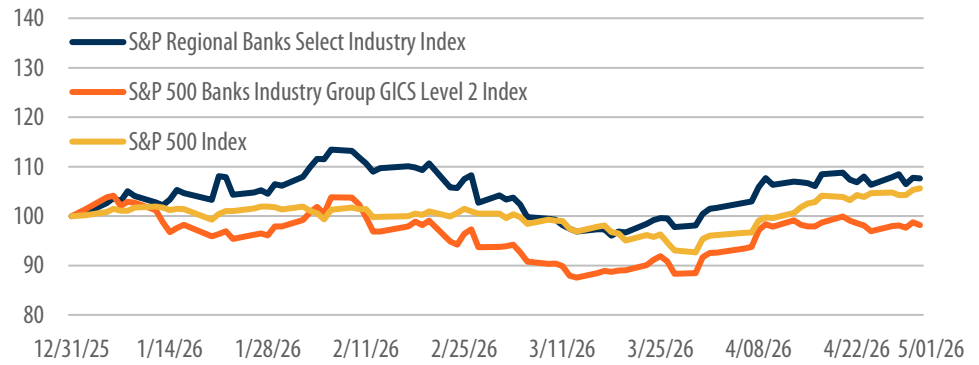
This chart is for illustrative purposes only and not indicative of any actual investment. The illustration excludes the effects of taxes and brokerage commissions or other expenses incurred when investing. Investors cannot invest directly in an index.

The S&P 500 Index is an unmanaged index of 500 companies used to measure large-cap U.S. stock market performance. The S&P 500 Banks Index is a capitalization-weighted index. The S&P Banks Select Industry Index comprises stocks in the S&P Total Market Index that are classified in the GICS Asset Management & Custody Banks, Diversified Banks, Regional Banks, Diversified Financial Services and Commercial & Residential Mortgage Finance sub-industries. The S&P Regional Banks Select Industry Index is comprised of stocks in the S&P Total Market Index that are classified in the GICS regional banks sub-industry.

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Regional Banks | Strong In 2026

Price Returns 12/31/25 – 5/1/26



Source: Bloomberg. S&P Dow Jones Indices. Daily price returns, normalized to a factor of 100. Past performance is no guarantee of future results.

View from the Observation Deck

The FDIC reported that total assets held by the 4,336 commercial banks and savings institutions it insures increased by \$1.2 trillion year-over-year to \$25.3 trillion in 2025. While the largest banks hold the majority of these assets, regional and community banks comprise the lion's share of individual U.S. banking institutions. For example, the FDIC insured 3,909 community banks, representing \$2.8 trillion in deposits in 2025. Since the unexpected demise of Silicon Valley Bank in March 2023, the profitability of regional banks, which the Federal Reserve ("Fed") defines as organizations with total assets of \$10 billion to \$100 billion, has been the topic of much debate. For today's post, we set out to examine several potential catalysts behind the recent surge in equity valuations within the regional banking subsector and discuss potential barriers to near-term growth.

The S&P Regional Banks Index increased by 8.45% on a total return basis year-to-date (YTD) through 5/1/26. For comparison, the S&P 500 and S&P 500 Banks Industry Group Indices saw total returns of 6.00% and -1.01%, respectively, over the same time frame.

According to the federal funds rate futures market, investors estimate the Fed will no longer cut its benchmark interest rate in 2026 (as of 5/1/26), down from expectations of at least two cuts on 12/31/25. Banks earn a profit on the spread between interest paid and interest earned on deposits, over time. In our view, buoyant policy rates are likely to reinforce current banking sector profitability. Net interest margin (the difference between interest and dividends earned on interest-bearing assets and interest paid to depositors and other creditors) of all FDIC-insured community banks surged to 3.65% in 2025, up from 3.34% in 2024.

Regional bank valuations are attractive compared to their peers and the broader market.

The S&P Regional Banks Index's forward 12-month price to earnings (P/E) ratio was 10.71 on 5/1/26, compared to P/E ratios of 12.24 and 20.71 for the S&P 500 Banks Industry Group Index and the broader S&P 500 Index, respectively, as of the same date.

Final outcomes of proposed Basel III "Endgame" capital requirements remain unknown.

When we last covered this topic in 2024, Basel III regulations were estimated to raise capital requirements among the largest U.S. banks by 9%, representing a significant reduction in assets that could be utilized to generate profit. These estimates have fallen drastically in recent months, with Reuters reporting a proposed increase of just 1.4% as of March 2026. That said, there is no guarantee regulators will agree to the proposal.

Takeaway

The S&P Regional Bank Index is off to a strong start this year, increasing by 8.45% (total return) YTD through 5/1/26. In our view, this performance is likely explained by buoyant profit expectations driven by stable Fed policy rates. Net interest margins increased in 2025, with FDIC-insured banks seeing the metric increase to 3.30% in 2025, up from 3.22% in 2024. Margins improved among community banks as well, with net interest margin increasing to 3.65% in 2025, up from 3.34% in 2024. While diminished, regulatory risks remain, with the largest U.S. banks seeking clarity regarding the impact of proposed Basel III capital requirements. Commercial real estate (CRE) exposure poses a potential risk to smaller banks, with the share of CRE loans held by community banks that were 30 days or more past due (or in nonaccrual status) increasing to 1.19% in Q4'25. While headwinds exist, we believe regional banks and community banks are pivotal to the economic growth of the locales they serve and are vital to a competitive and resilient banking system.