Investment Strategy

Silicon Valley Bank (SVB)

Developments in the financial sector and regional banks in particular have been rapidly unfolding over the past week. The news has raised questions about some of the larger banks that were deemed systemically important by the Financial Stability Oversight Council, established in 2010 under Dodd-Frank.

In terms of what happened to the banks that have been in the news, they were subject to large scale withdrawals by depositors in a very short time frame. This came after a period when they took large scale deposits, also in a relatively short time frame, and invested them in loans and fixed income securities. In the case of Silicon Valley Bank (SVB), the institution was forced to sell assets at a loss to meet redemptions resulting in impaired capital ratios. Some variation of that (or fears of a similar situation) appears to be the case at other institutions with similar profiles. The issue cascaded, with more depositors wanting to withdraw more funds. This is fundamentally different than the 2008-2009 Global Financial Crisis when banks held compromised assets, while this appears to be more of a mismanagement of liquidity issue.

The regulatory authorities have responded aggressively deeming both Silicon Valley Bank and Signature Bank systemically important giving them wide ranging authority to wind the banks down. They are also guaranteeing depositors at the institutions full access to their deposits and establishing a separate facility (Bank Term Funding Program) to aid certain financial firms affected by the market instability (if necessary). These steps are important in terms of providing confidence, a liquidity backstop, and most importantly, time.

The regional banks in the news are different than the large money center banks such as BNY/Mellon, Bank of America, Wells Fargo, JP Morgan/Chase etc. The larger banks have been subject to increased oversight, periodic stress tests, and limitations on business lines (the Volcker Rule) in the wake of the Global Financial Crisis. They have much more diverse business models and were already deemed systemically important, giving the Treasury Department authority to unwind them in a way that it has previously said, “fully protects all depositors” if necessary. Current market prices of the securities of these larger banks (such as credit default swaps and bonds seem to indicate that the market understands these are different than the regional banks in the news.

This recent event is a stark reminder of why paying attention to FDIC limits is critical in terms of protecting certificate of deposit holdings from these types of situations. The regulatory authorities are sensitive to all size depositors, but the FDIC insurance provides a high degree of comfort where applicable.■