

INVESTOR NEWSLETTER

AFTER SVB COLLAPSE

So the FED has been tightening by raising interest rates so far but given the most recent shock to the system in the form of shut down of Silicon Valley Bank followed by news about Signature Bank, is the FED going to kill the market.



WHAT MIGHT THE FED DO?

Technically, the FED should act independent of any market movements because its main job is to keep the economy stable by ensuring that inflation does not get out of hand. But if the financial system gets derailed, keeping the economy stable is going to be a much bigger challenge and inflation will definitely become priority number 2; not 3 or 4 or any other later number, just 2.

So priority number 1 is, keep the financial system in place. Are the higher interest rates only to blame for the collapse of SVB? The answer seems to be 'No' so far. Startups are riskiest of all asset classes and when a bank has a symbiotic relationship with mostly startups then there is bound to be a run on the bank when things go south. Why? Because the startups consume more money than they generate. The riskier the environment, the more panicky they'll get and the higher the chance they'll all need to get their deposits at the same time. Startups by definition do not have much of a backup plan and when the cash you are sitting on is the only backup plan of startups then good luck trying to explain to them that your money is in John's house and John's money is in Suzie's house.



So far the US authorities seem to be assuring people that their money is safe even after the collapse of SVB and the likes. Do the US authorities have the capacity to fund all the deposits of all the banks that are in trouble? It is yet to be seen. A lot depends on how big is the bank run and how quickly the panic can be subdued.

So far the inflation figures are looking alright with the latest CPI number in line with expectation at around 6%. As a result, people are hoping the US FED will stop further rate hikes and hence cause fewer bankruptcies of institutions like SVB.