
Greg Hague
RECENT BANKING
INDUSTRY
DEVELOPMENTS
Learn what they are and what they mean for home sellers.

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INVERSE RELATIONSHIP BETWEEN BOND PRICES & MARKET INTEREST RATES

Because bonds have stated fixed interest rates, and are traded on the open market, the primary way bond purchasers get a higher interest rate (when rates are going up) is to purchase the bond below its face value.

When the Fed raised interest rates so quickly, bond values (prices on the open market) dropped accordingly, making the asset value of banks that held them decline quickly.

This caused depositors of SVB to become nervous and withdraw $40 billion in one day.

SVB had to sell the bonds (treasuries) it owned to pay depositors, thereby suffering massive losses that were "on the books" but had not actually been realized.

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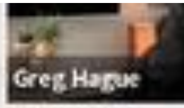

SVBs deposits had been declining since late 2022. Withdrawals were accelerating in Jan and Feb of 2023 because high growth tech companies were maintaining burn rates but were unable to tap new investor money as easily as they had in prior years.

SVB announced Wednesday (March 8th) that they sold bonds at a loss. The $40 billion was drawn out on Thursday (March 9th) largely in response to that disclosure and a subsequent failure to raise additional capital via a stock sale.

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The Fed immediately stepped in and did something it does not typically do... guaranteed the deposits of all depositors, even those over the $250,000 FDIC minimum. It did this by tapping the "Deposit Insurance Fund" that all FDIC-insured banks are required to contribute to, so no tax dollars were used.

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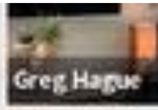

TWO POINTS TO EMPHASIZE

1 While the FDIC has never implemented a blanket coverage of $250k plus, they did cover 100% of some transaction accounts with much larger balances in 2008.

2 More importantly, the Deposit Insurance Fund is not new and was not created in response to SVB. It was created many years ago to fund any losses from the $250,000 FDIC deposit insurance.

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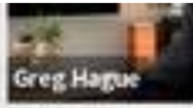
WHY DID THE FED COVER MORE THAN $250,000 OF DEPOSITS WITH SIGNATURE AND SVB?

The Fed did this because it feared Americans with large bank deposits would withdraw them, forcing thousands of banks across the country to liquidate billions in bonds at massive losses and thereby destabilize the entire banking industry.



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THIS LEAVES A LOT OF LOOSE ENDS TO TIE UP...

01 Who will be able to access the Deposit Insurance Fund? Does this mean all uninsured deposits are now de facto insured? If so, how long will that last?

02 Will there be any new regulation on medium-sized banks to go along with the implicit deposit guarantee? Should there be?

03 Was this a “bailout”? Does it matter?

04 What will be the long-term effects of this on the relationship between the U.S. government and the VC/startup industry?"

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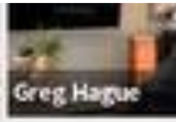

"What this means is that the Fed, by raising interest rates, is making our banking system less stable. Under normal circumstances, the Fed would respond to this week's events by simply cutting rates — just like it did for 40 years. But there's a reason it can't easily do that this time — inflation hasn't gone away."

– NOTED ECONOMIST NOAH SMITH

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IN CONCLUSION...

POSSIBLE SAFETY

The new Federal Deposit Insurance fund applied to all bank deposits (not just SVB and Signature) might allow the Fed to safely further raise rates.

MY PREDICTION

I think the Fed will not immediately apply FDI to all deposits and will moderate its predicted 1/2% raise to 1/4%, then monitor things closely, knowing it can apply FDI to all banks, or troubled banks, as needed.