



March 21, 2023

Investment Commentary

Have the Cockroaches Infested the U.S. Banking System?

I spoke with [The Wall Street Journal](#) on Friday, March 10th. One of the newspaper's editors, Christina Rexrode, had asked Matt Grossman, a reporter on her bank-specialized staff, to call me. She and I had spoken several times on banking issues in the last few years. I thought I could interrupt lunch for a call from [The Wall Street Journal](#). Grossman was interested to determine whether the collapse of the [Silicon Valley Bank \(NASDAQ: SIVB\)](#) was a systemic or unique issue. The word he used for unique was, according to my colleague, Brian Valencia, "idiosyncratic," a word which I interpreted to be unique enough not to cause concern about any sector issue. Nevertheless, the word is not part of my every day or functional vocabulary, and I quietly asked Brian, who was attempting to consume a turkey and cheddar sandwich that we had bought at Stonehorse Market, whether he agreed with my definition, and he gave me a thumbs-up.

"I think this could be the first cockroach in the cellar," said Fredric Russell, chief executive of [Fredric E. Russell Investment Management Co.](#) in Tulsa, Okla. "Banks get thrown into the dark pool of complacency, and then they lower their quality standards."

Of course, when interest rates rise all banks are challenged but I told Grossman that the [Silicon Valley Bank](#) was suffering an unusual outflow of deposits, a situation that I thought was unique and reflected a huge outflow of deposits accelerated by the fear of crypto-based lending. After quoting me, Grossman continued:

"The crisis deepened on Sunday while also showing early glimmers of stabilization. Regulators took control of [Signature Bank](#), a New York lender with \$110 billion in assets, marking the third bank collapse in a week. But stock futures rose in Asian trading after the U.S. government announced measures aimed at easing concerns among depositors and making more funding available to the banking system. Banks, especially the largest, are much better capitalized than they were heading into the 2008 financial crisis. Still, some investors worry that the problems now slamming a few regional banks could affect the whole industry. The Federal Deposit Insurance Corp. insures depositors with up to \$250,000 in cash at a bank. In the cases of [SVB](#) and [Signature Bank](#), officials took the extraordinary step of designating the banks as a systemic risk to the financial system, which gives regulators flexibility to backstop uninsured deposits. The Federal Reserve and the Treasury Department also used emergency lending authorities to establish a new facility to help meet withdrawals." *Grossman, Matt. "SVB Crisis Heightens Investor Worries." [The Wall Street Journal \[New York City\]](#), March 13, 2023, page B1.*

March 14, 2023

Charles Schwab CEO Walt Bettinger said Tuesday that his firm is still experiencing sizable inflows, contrary to fears that the banking crisis brought on by the **Silicon Valley Bank** collapse is spreading in the sector.

“What we’re seeing is asset inflows to the firm in significant numbers,” Bettinger told CNBC’s Sara Eisen on “The Exchange.”

He said **Schwab** clients moved almost \$42 billion in net new assets to the firm in February. Month to date, they’ve averaged about \$2 billion a day, the CEO said.

Meanwhile, Bettinger revealed he bought 50,000 shares Tuesday morning for his personal account. “That much confidence I certainly have in this company,” he said. Those shares are worth nearly \$3 million at Schwab’s open price Tuesday.

“What I’ve heard from the advisors that I spoke with yesterday is great confidence in our firm. ... They know how conservative we are. They know we don’t take risks,” Bettinger said. “That’s why we don’t go out a long way in terms of duration, and that’s why we maintain access to liquidity in the way that we do.”

“Our bank is very conservatively managed. If you look into the holdings of the bank, we have about 10% of client deposits outstanding in loans,” Bettinger said.

Li Yun from CNBC finishes, “The demise of **Silicon Valley Bank**, as well as crypto-focused Signature Bank, prompted extraordinary rescue action from regulators and caused a financial shock that rocked markets, especially shares of regional banks. In addition to backstopping the deposits at SVB and Signature Bank, federal regulators also announced an additional funding facility for troubled banks.” *Li, Yun. “Charles Schwab CEO says firm is seeing significant inflows and that he bought the stock Tuesday.” CNBC, March 14, 2023, <https://www.cnbc.com/2023/03/14/charles-schwab-ceo-says-firm-is-seeing-significant-inflows-even-as-stock-gets-hit-during-banking-selloff.html>. Accessed March 20, 2023.*

We do not use **Schwab** as a bank. In fact, we do not use any bank. We do not borrow money for our clients nor for ourselves. **Schwab** executes orders for us, holds client securities, and when we are not investing in equities, we make a practice of buying United States Treasury obligations so that virtually no cash is held above the S.I.P.C. (S.I.P.C. insures brokerage accounts, which includes any of your accounts with us and F.D.I.C. covers bank accounts.) insured amount of \$250,000.

Brian Valencia and Alaina Hall helped me with some of the background research for this letter.

Sincerely,



Fredric E. Russell, CEO