TELEPHONE (615) 255-6431
FACSIMILE (615) 244-7646

INVESTMENTS SINCE 1945
MEMBER SIPC

WILEY BROS.
AINTREE CAPITAL, LLC

40 BURTON HILLS BOULEVARD

NASHVILLE, TENNESSEE 37215

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For most of us, the words “bank failure” immediately trigger the same memory: the financial crisis of 2008. That was a year no investor could ever forget. The year some of the largest, most storied financial institutions in the world – think Lehman Brothers, Bear Stearns, and others – collapsed, never to return.

Similarly, for anyone who has studied history, the words “run on the bank” immediately trigger images of the early days of the Great Depression. For others, perhaps it’s scenes from *It’s a Wonderful Life* (or *Mary Poppins*, if you prefer). Dramatic moments now consigned to the waste bin of time. Surely not something that could happen in *this* day and age.

But last month, all these words – bank failure, bank run – happened.

As you know, Silicon Valley Bank (SVB) was seized by federal regulators on Friday, March 10. It was not the first bank to collapse this month, nor was it the last. Two days earlier, Silvergate Bank, another California institution, announced it would liquidate its assets and wind down operations. And two days after the SVB collapse, regulators closed a *third* bank. This was Signature Bank, based out of New York.

What do these banks have in common, besides sharing a similar fate? Well, all three were hit by bank runs in the days prior to their collapse. All three had made ill-timed investments in recent years. For Silvergate and SVB, this was in the form of overexposure to government bonds, which dropped in value as interest rates skyrocketed. For Signature – and Silvergate, too – the trouble really started when the price of bitcoin and other cryptocurrencies plummeted in 2022.

In response, investors, not to mention the many companies with their deposits on hold, waited with bated breath to see what the government would do. After all, everyone still remembers what happened in 2008. Back then, panic spread across the entire banking industry – and from there to the overall economy. Unfortunately, some of that panic came because the government stepped in and then didn’t, which left investors with uncertainty.

“Contagion” is a very real thing when it comes to banking, and no one wants a repeat of the financial crisis. In recent days, other banks that have *not* collapsed, have strong balance sheets, and are not necessarily in danger, still saw their stock prices fall dramatically. This partly came due to how connected individual stocks are with index fund trading and partly because investors run if they catch even a whiff of financial instability.

As it turns out, Washington moved swiftly and decisively in an attempt to stamp out uncertainty. On March 12, the Federal Reserve created the **Bank Term Funding Program**. This program will provide emergency loans for up to one year to safeguard 100% of deposits to any bank or credit union that needs it.[1] (Normally, only the first $250,000 of an account’s deposits were insured against loss. Most of the organizations doing business with these three banks stood to lose much, much more than that.) In return, these banks must put up any Treasuries or highly rated debt they own as collateral and pay a modest interest rate.

The idea here is to stabilize all the regional banks around the country by assuring customers their money is safe. Furthermore, the program is designed to make it easier for banks to get needed liquidity instead of selling their assets off in a fire-sale.

A couple things to note about this program:

First, this is not a "bank bailout" in the traditional sense. The banks themselves are not being saved or spun off to other, larger banks. Furthermore, both bond- and stockholders of these banks will still likely experience a loss in the short term. This program is designed solely to protect depositors. (Of course, the exact definition of a "bailout," and whether one is justified or not, is a topic best left to politicians.)

Second, to pay for all this, the government will draw from the **Deposit Insurance Fund**. This fund comes from quarterly fees levied on financial institutions. Public taxes will not be used.[2]

So, what does all this mean for the future? What does it mean for us?

There are several things we as investors need to be aware of:

1. More volatility. The government's actions temporarily stabilized the markets. But the major indices dropped again when an important *European* bank, Credit Suisse, was found to be in financial difficulty, albeit for different reasons and has been in decline long before these failings. In the short term, investors will be hypersensitive to *any* banking instability. That means volatility is still very much in the cards. Credit Suisse was quickly taken over by UBS.
2. Politicization. Right now, politicians and pundits on both sides of the aisle are trying to turn this issue into the latest political football. As investors, we must avoid getting caught up in all that and remain focused on keeping to our investment strategy.
3. Interest rates. There's a lot of chatter on Wall Street right now that this issue will cause the Federal Reserve to delay more interest rate hikes. If that happens, it's quite possible the markets will go up. But *we do not make guesses* about which way the markets will go or what the Fed will do short-term. In fact, you can make an argument that doing so is partly why SVB got into so much trouble.

Obviously, there's a lot my team and I will be monitoring in the coming weeks. In the meantime, my advice to you is to enjoy the start of Spring! Whenever anything changes, we'll let you know immediately. And as always, do let me know if you have any questions or concerns.

Have a great month!

Sincerely,

Robert G. Elliott, CFP
Vice President

Sarah L. Elliott, CFP

[1] "Federal Reserve Press Release," March 12, 2023. https://www.federalreserve.gov/newsevents/pressreleases/monetary20230312a.htm

[2] "Wall Street – not taxpayers – will pay for the SVB and Signature deposit relief plans," *CNBC,* March 12, 2023. https://www.cnbc.com/2023/03/13/wall-street-not-taxpayers-will-pay-for-the-svb-and-signature-deposit-relief-plans-.html