Capital Markets Strategy
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MUFG

Policy Note

Silicon Valley Bank: An Outlier Among Peers

Unusually large bank, below more stringent TBTF regulatory threshold
16th largest US bank, but $210 bn assets below $250 bn "systemically significant" threshold

"Niche" business, heavily reliant on Tech / VC / life science
Non-traditional deposit base, low loan-to-deposit ratio

Large, non-traditional deposit funding base
Less than 10% of deposits from "stickier" domestic retail; largely tech / VC

Low loan-to-deposit ratio
Smaller lending book given tech / VC customer base; therefore larger securities portfolio

Large HTM investment portfolio
Investment portfolio heavily HTM, more vulnerable to mark-to-market in event of forced asset sales

Unusually high exposure to rate risk in long duration portfolio
Large HTM portfolio in higher yielding, longer duration USTs & MBS over Fed reserves and T-Bills

SVB was an outlier among its peer group in terms of size, customer profile and investment imbalances. While a few regional banks of similar risk profile could also come under pressure, we believe the US banking system in aggregate is very strong. The "unintended consequences" of a large bank failure are also difficult to anticipate.

Largest Post GFC Bank Failure: With $210 bn of assets (2/3 of Washington Mutual), SVB was the 16th largest US bank, and the largest to go into FDIC receivership since 2008. Regulators noted both inadequate liquidity and insolvency in the decision to shut down the bank.

Deposit Surge: US venture capital-backed technology companies raised $330 bn in 2021, double the prior year. SVB's deposit base doubled from $62 bn to $124 bn in just 12 months, triple the rate of deposit growth at large US money center banks.

Non-Traditional Deposit Base: Less than 10% of SVB's $172 bn deposit base came from "stickier" US domestic retail, with an unusually high reliance on technology / VC / early stage health science. Nearly 90% of deposits were uninsured, also an outlier among peers.

Deposit Run: As capital losses became more apparent, depositors tried to withdraw $42 bn of deposits on Thursday, March 9 (in addition to $25 bn of deposit outflows in prior quarters). SVB's share price declined 60% the same day before trading was halted.

Low Loan-to-Deposit Ratio: Less demand for loans from SVB's "niche" technology / VC / life sciences customer base, who don't have the high fixed asset, reliable cash flows characteristic of high quality borrowers. SVB's large deposit surge was therefore invested largely in higher yielding, longer duration USTs and agencies.

For most banks, higher interest rates can drive stronger earnings as loan rates rise more quickly than deposits. However, the opposite was true for SVB. Given the unique attributes of its customer base and business profile, SVB had a comparatively small lending book, and therefore very large investment portfolio, which they invested largely in longer duration, fixed rates securities.

Large HTM Securities Portfolio: SVB also held a very large amount of its securities portfolio in the "Held-to-Maturity" (HTM) bucket, which resulted in a large part of the investment portfolio being suddenly "marked-to-market" when the Bank was forced to sell securities. Since 2019, SVB's "available-for-sale" (AFS) book doubled from $14 to $27 bn, while its HTM book grew from $14 to $99 bn.

Longer Duration Investment Portfolio: SVB had unusually high exposure to interest rate risk. In the absence of a vibrant lending business, SVB invested in longer duration USTs and MBS over Fed reserves and shorter-dated T-Bills. 56% of SVB's assets were invested in fixed rate securities (large money center banks < 30%). Avg maturity of SVB HTM bond portfolio was 6.2 years at end of 2022.

Large Mark-to-Market Losses: By the end of 2022, with inflation / Fed tightening / rates markedly higher, SVB had mark-to-market losses above $15 bn for securities held-to-maturity, which exceeded its $11.8 bn tangible common equity. Portfolio marks and losses rose on forced asset sales as depositors ran.

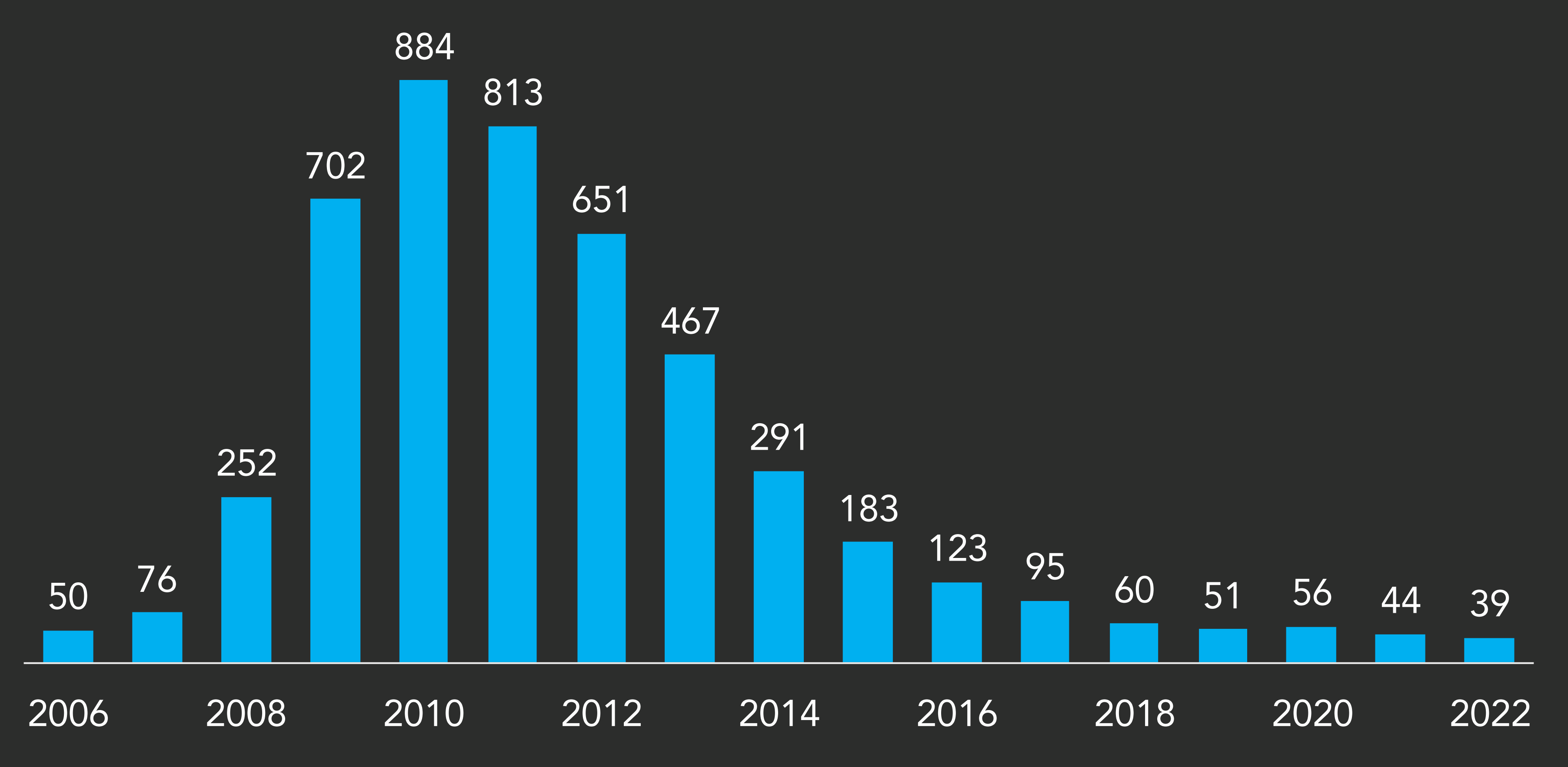
ALM Policy Errors: Questions remain as to (1) why SVB did not more effectively manage the ALM issues on the asset side as interest rates rapidly increased; and (2) why they did not move to raise capital sooner.

FDIC Receivership: Before 9am local time on Friday, March 10, the California Department of Financial Protection and Innovation closed SVB, appointing the FDIC as receiver.

Treasury, Federal Reserve, FDIC Action: On Sunday, the Treasury, Federal Reserve, and FDIC jointly announced actions to strengthen financial stability and limit broader contagion. First, Treasury Secretary Yellen instructed the FDIC to make all depositors, including those uninsured, whole. Secondly, the Fed announced a new "crisis-era-like" Bank Term Funding Program (BTFP) to provide banks up to 12 months financing with qualifying assets used as collateral valued at par rather than mark-to-market. Lastly, the Fed will also accept collateral at par value at the discount window.

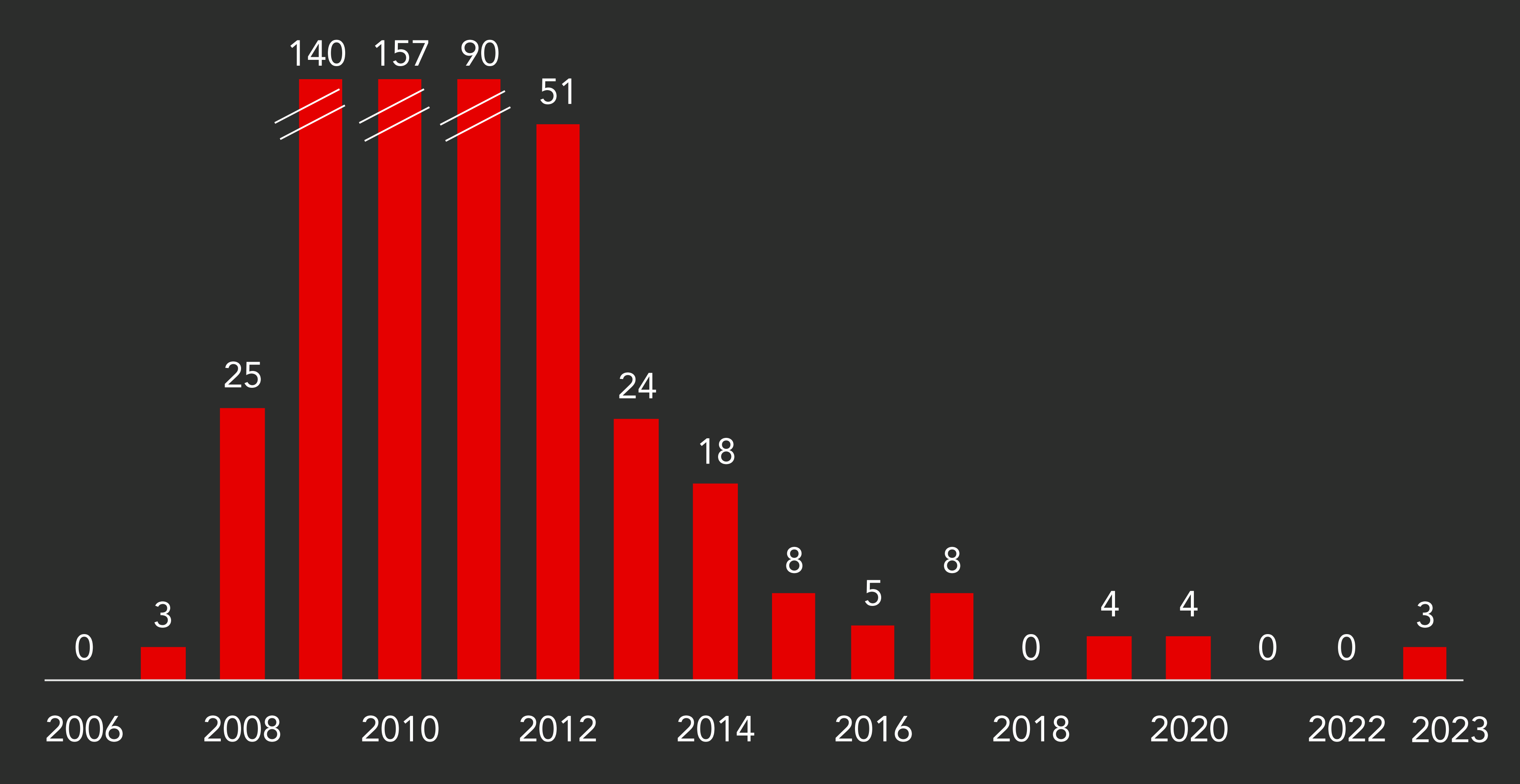
Silicon Valley Bank was not even included among the 39 banks on the FDIC's "Problem Bank" list at the end of 2022. Problem Banks are those whose financial condition are rated 4 or 5 on the CAMEL regulatory rating system (acronym derived from capital, asset quality, management, earnings and liquidity). SVB arguably should have failed on 3 of 5 categories (C, M and L).

# of banks on FDIC's "problem institutions" list



During the peak of the global financial crisis (GFC), more than 300 US banks failed between 2008-2010. Silvergate Capital, Silicon Valley Bank and Signature Bank became the first three US banks to fail in three years (since 2020).

# of failed FDIC institutions



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Federal Reserve's Bank Term Funding Program (BTFP) Terms

Eligible Borrowers:	US federally insured depository institutions or US branch or agency of a foreign bank eligible for primary credit
Eligible Collateral:	Any collateral eligible for purchase by the Federal Reserve in open market operations, as long as it was owned prior to March 12, 2023 (includes USTs, agency debt and MBS)
Advance Size:	Value of eligible collateral pledged by the borrower
Collateral Valuation:	Collateral will be valued at par. Margin will be 100% of par value.
Rate:	1 year OIS + 10 bps, fixed for the term of the advance on the day the advance is made
Prepayment:	Allowable at anytime without penalty
Term:	Up to one year
Program Duration:	At least March 11, 2024
Fees:	No fees
Recourse:	Advances made with recourse beyond the pledged collateral to the eligible borrower
Credit Protection:	The Treasury would provide $25 bn as credit protection to the Federal Reserve via the Exchange Stabilization Fund

Source: FDIC. Company Filings. Bloomberg. WSJ. Capital Economics. Oxford Economics.

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