CORE Comments
ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

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The Collapse of Silicon Valley Bank—
—What does it Portend for Assets
At Brokerage Firms like Schwab?

On Friday, the Federal Deposit Insurance Corporation (FDIC) took control of Silicon Valley Bank (SVB), after a run by its depositors to withdraw their funds. The FDIC insures bank deposits up to $250,000 per account; SVB had some $175 billion of deposits as of the end of 2022, but only a very small percent—some 3%—were under $250,000 and insured by the FDIC. Because SVB's assets, (its loan book and other investments) were worth less than its liabilities (its customers deposits), it was at risk of insolvency. As this became know, its depositors rushed to withdraw their funds, some $42 billion on Thursday alone!

In a short time, we will know what the FDIC will do with SVB; it may try to sell it a large bank like JP Morgan Chase or Bank of America. I write not to discuss SVB, but to address the questions you may have about the safety of your assets at Schwab and other brokerage firms. Brokerage firms have an insurance scheme different to those of banks. The Securities Investor Protection Corporation (SIPC) is a federally-mandated, privately-owned entity that insures customer deposits at brokerage firms. Its coverage is $500,000 per account. In addition, most large brokerage firms, including Schwab, have joint arrangements with Lloyds of London and other private insurers to provide coverage up to $600 million per account. These come in to play in the event of insolvency of the brokerage firm or in other circumstances.

As you will not be surprised to read, customer accounts of brokerage firms and banks are segregated from those firms' own assets. Beginning in November last year, we learned about the commingling—better called theft—of customer assets at the crypto firm FTX and its affiliate Alameda, the organizations of Sam Bankman-Fried. Crypto matters operate in a different universe from US banks and US brokerage firms. Do not conflate the crypto universe with the one in which we conduct our lives.

Customer assets held by Chase, by Schwab and by other banks and brokerage firms are segregated from the assets owned by these companies for their own accounts. SVB got in trouble because its customer deposits grew at a spectacularly rapid pace in the last couple of years while demand for loans was weak in Silicon Valley. Because of relatively weak loan demand, SVB invested a good deal of its customer deposits in Treasury bonds. These Treasuries were, of course, safe from a credit point of view—the United States does not default on it debts. But the Treasuries lost value as the Fed raised interest rates so sharply in the last year. As SVB depositors withdrew their funds recently, SVB was forced to sell some of its

By

Jack Mayberry

assets to fund those withdrawals. Some of those assets were sold at a loss and SVB faced insolvency.

We recently changed our post office box in Sausalito to PO Box 866.

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Some other mid-sized banks apparently have problems akin to those at SVB, so we made read of more bank problems. Treasury Secretary Janet Yellen was on news programs today assuring us that US banks are well capitalized. If we should learn of other banking problems in the weeks ahead, we should not conclude that our assets at Schwab or other brokerage firms are at risk. Your accounts many gain or lose value according to our success and lack of success in managing your assets. But your assets are not at risk from failures or weaknesses at Schwab or elsewhere. The SIPC and private insurance that Schwab and others hold removes that risk.

I intend to write a general letter about our investments soon. To foreshadow the letter to come: I still think that a recession is inevitable; I expect the Fed to keep raising rates; I expect that bonds will rise in price in the next year; I think that the stock market has further to fall. Your portfolios are positioned to benefit from the outcomes I foresee. As it happens, on Thursday and Friday, when the markets were shaken by the SVB matter, Core's clients' accounts rose by about two percent.

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CORE ASSET MANAGEMENT

PO Box 1629
108 Caledonia Street
Sausalito, California 94966
(415) 332-2000 • (800) 451-2240
fax (415) 332-2151
www.coreasset.com
info@coreasset.com