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Bank Bust:

Lessons Learned for All CUs & How Best to Manage Risk in an Unprecedented Market



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Emily Hollis
Co-founder & President
ALM First Financial Advisors



Tim Harrington, CPA
President
TEAM Resources



Daniel Lally
PR & Strategic Communications
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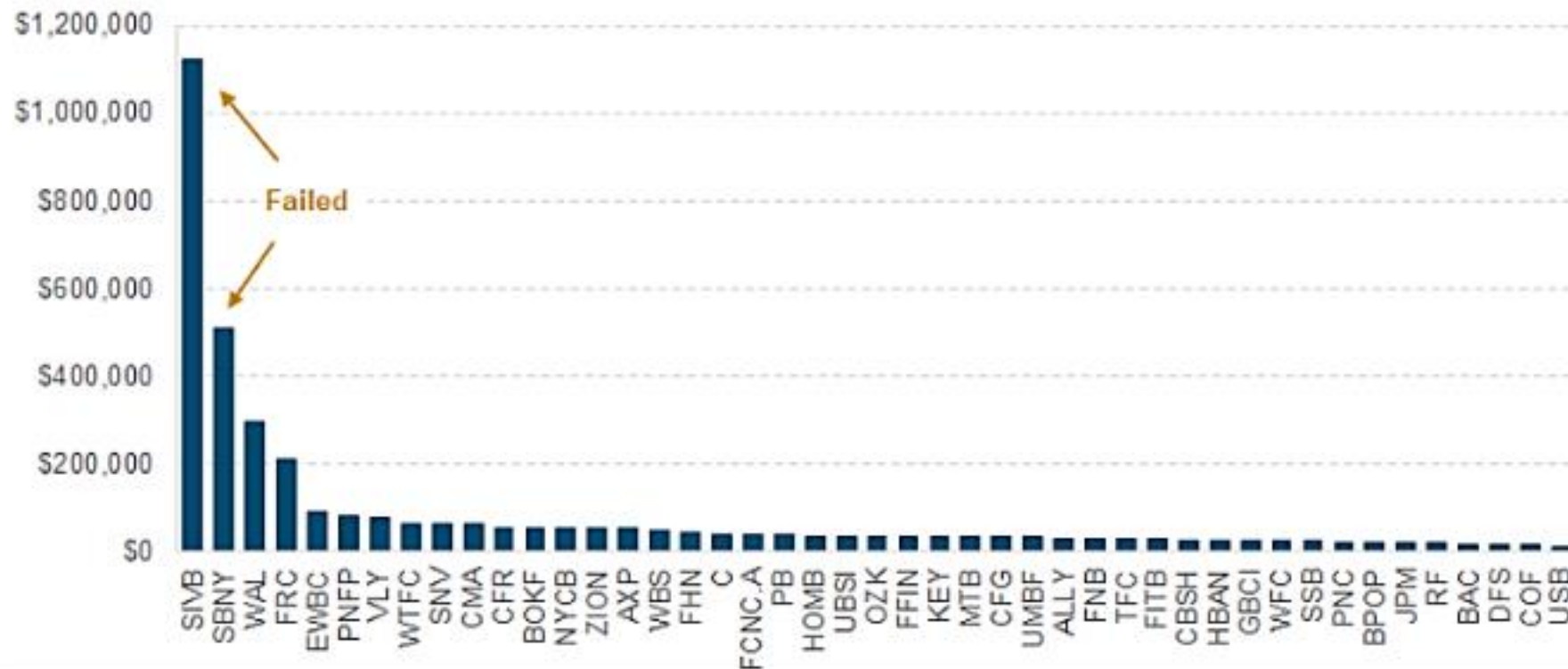
Bank Bust: ALM Lessons Learned for CU Leaders

Emily Hollis, Co-founder & President, ALM First Financial Advisors

Common Denominator

Deposit Size per Account

Major U.S. Commercial Banks: Average Deposit Size per Account

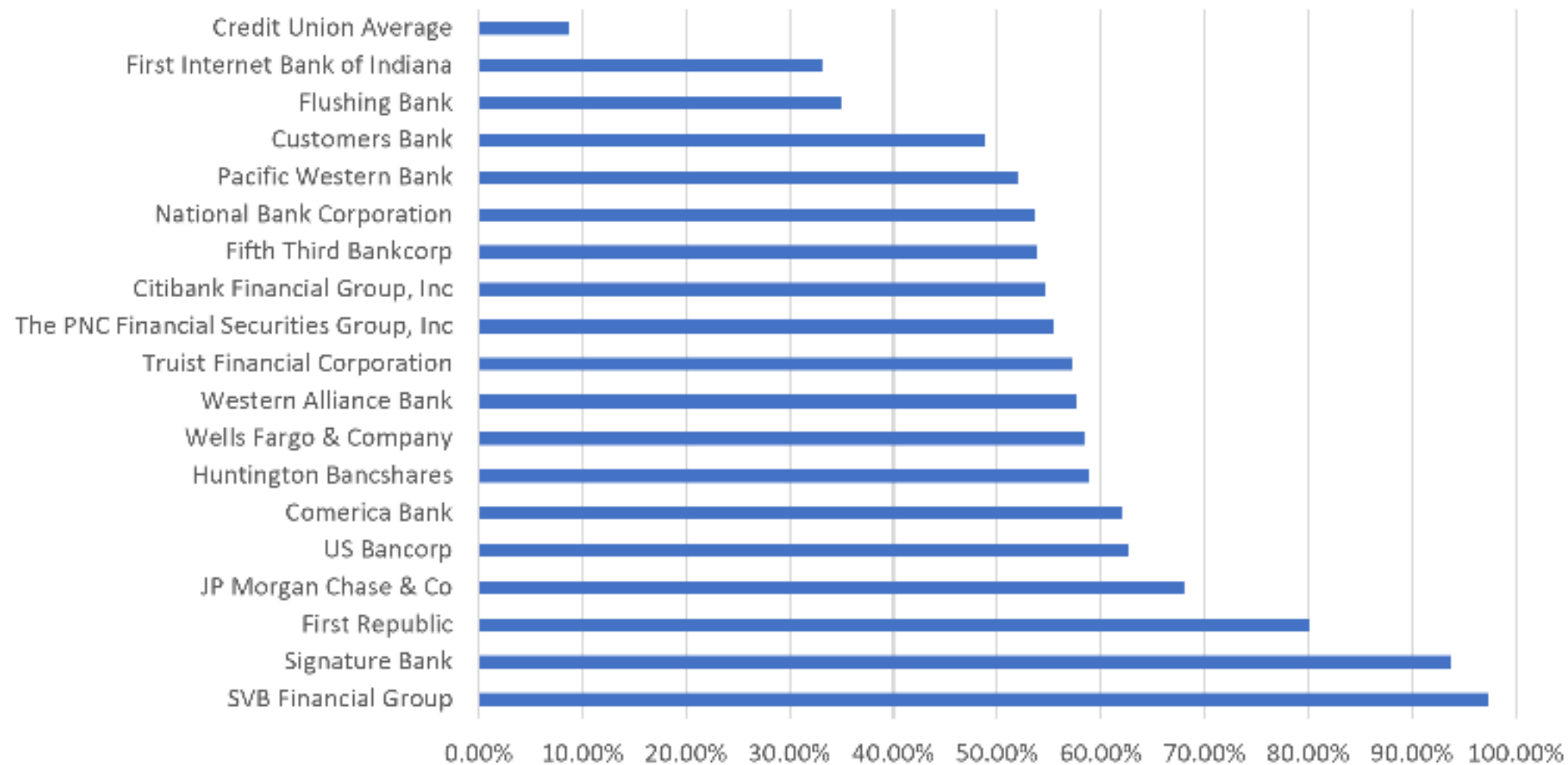


Source: FFIEC Call reports, S&P Capital IQ Pro, CreditSights

In \$, as of 4Q22

For top tier commercial bank entity only, ex. VTFC (aggregate across 15 entities) and USB (incl. Union Bank)

Uninsured Deposits



Silicon Valley Bank (SVB): What Really Happened?



A unique banking model

- Deposit base heavily concentrated in the tech sector – venture capital and startups
- That customer base was more cash-rich with less need for loans
- Fueled significant growth in assets for SVB in 2020-2021
- Bond portfolio accounted for nearly half of the balance sheet and was primarily comprised of longer duration Treasuries and Agency MBS (unhedged)



Questionable management decisions

- In addition to poor ALM practices in recent years, several questionable decisions were made during the week SVB failed
- In an apparent attempt to avoid an imminent downgrade by Moody's, SVB moved to sell its AFS portfolio, and the next day it would issue equity to replenish capital from the bond sales
- There was no evidence of a liquidity crunch prior to these steps, and SVB had ample borrowing capability
- The equity raise failed, and with essentially no public communication from the company explaining the steps, 25% of its deposits walked out the door (Game Over)

Idiosyncratic vs. Systemic

Silicon Valley Bank was a very specialized model, effectively serving as the banker for a struggling tech industry

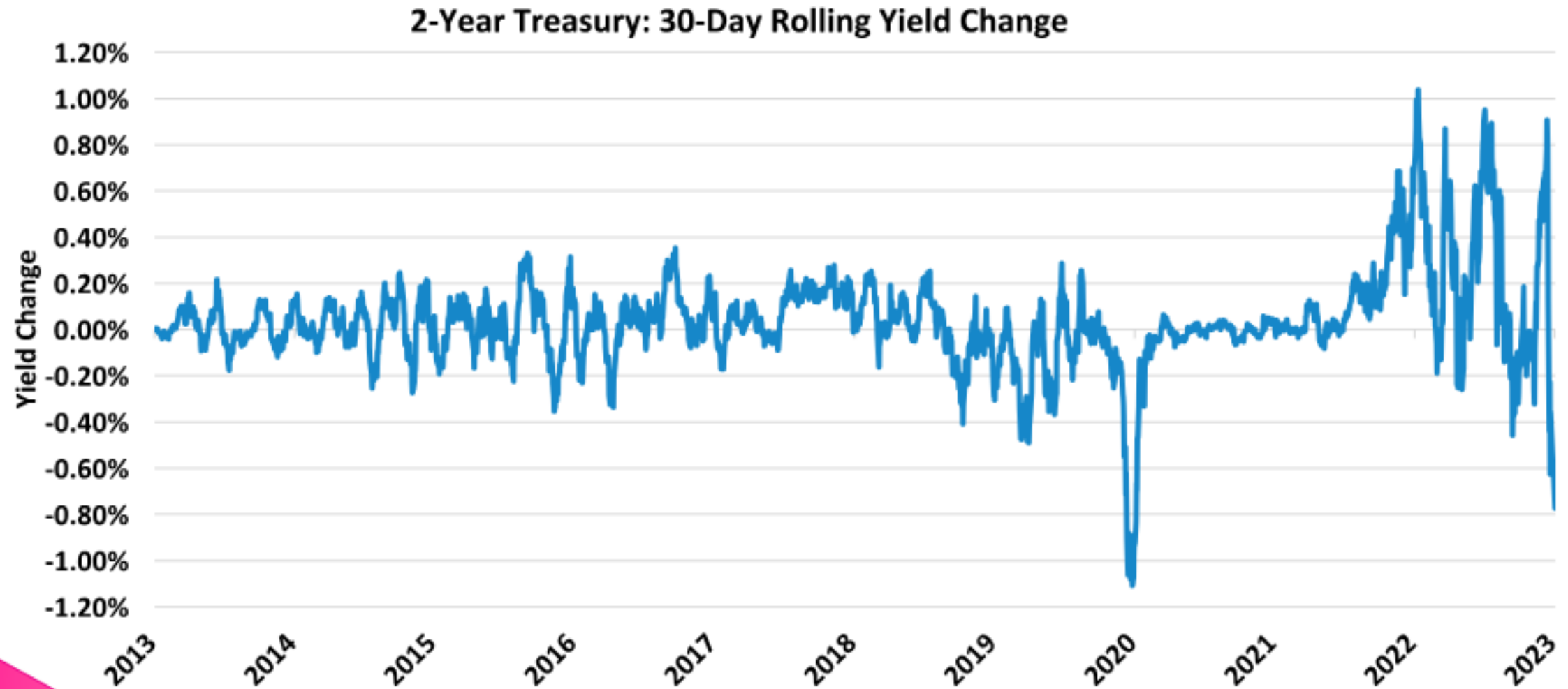
- The bank's securities portfolio accounted for half the balance sheet, and the bank made rate bets last summer during the "Fed pivot" speculation
- Heavy reliance on institutional deposits accelerated the "run"

System-wide, virtually all depository institutions have underwater financial assets

- Industry-wide capitalization and asset quality remain relatively sound, even after accounting for unrealized portfolio losses
- No institution can survive a run

"Whenever the Fed hits the brakes, someone goes through the windshield."

Extreme Rate Volatility



Next Steps

SLOW DOWN. Approach the current environment with caution

- Rates will likely be volatile, and pricing can become stale quickly.
- The risk is that you unintentionally end up “buying” the market in a certain type of asset class.
- It's OK to raise rates, slow/pause lending, and build a larger cash buffer than in calmer times until we receive more clarity on the environment in the coming weeks/months.

Risk premiums and expected returns should be higher

- Lending in today's market is different than 2 weeks ago.
- Make sure you are getting compensated for the enhanced spread and risk premiums that you are taking.

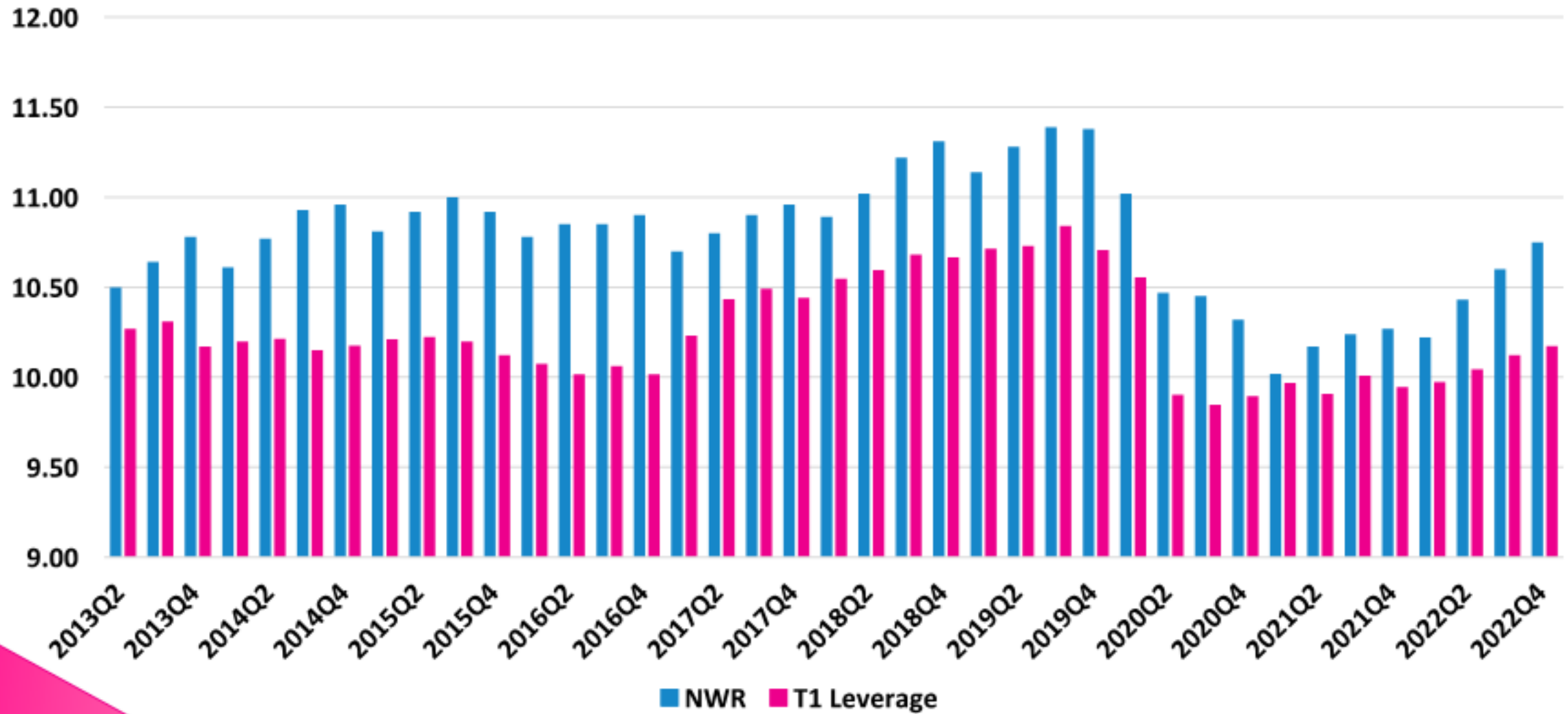
Hedge to lock in strong risk-adjusted pricing

- If you have properly priced loans, excess interest rate risk (IRR) can be mitigated through hedging.
- During volatile times, hedging can help you lock in your margins.

Continue to focus on prudent risk management—we are not out of the woods yet

- Identify and monitor unique risks to your institution
- Test your liquidity sources
- Focus on deposit betas, demographic analysis

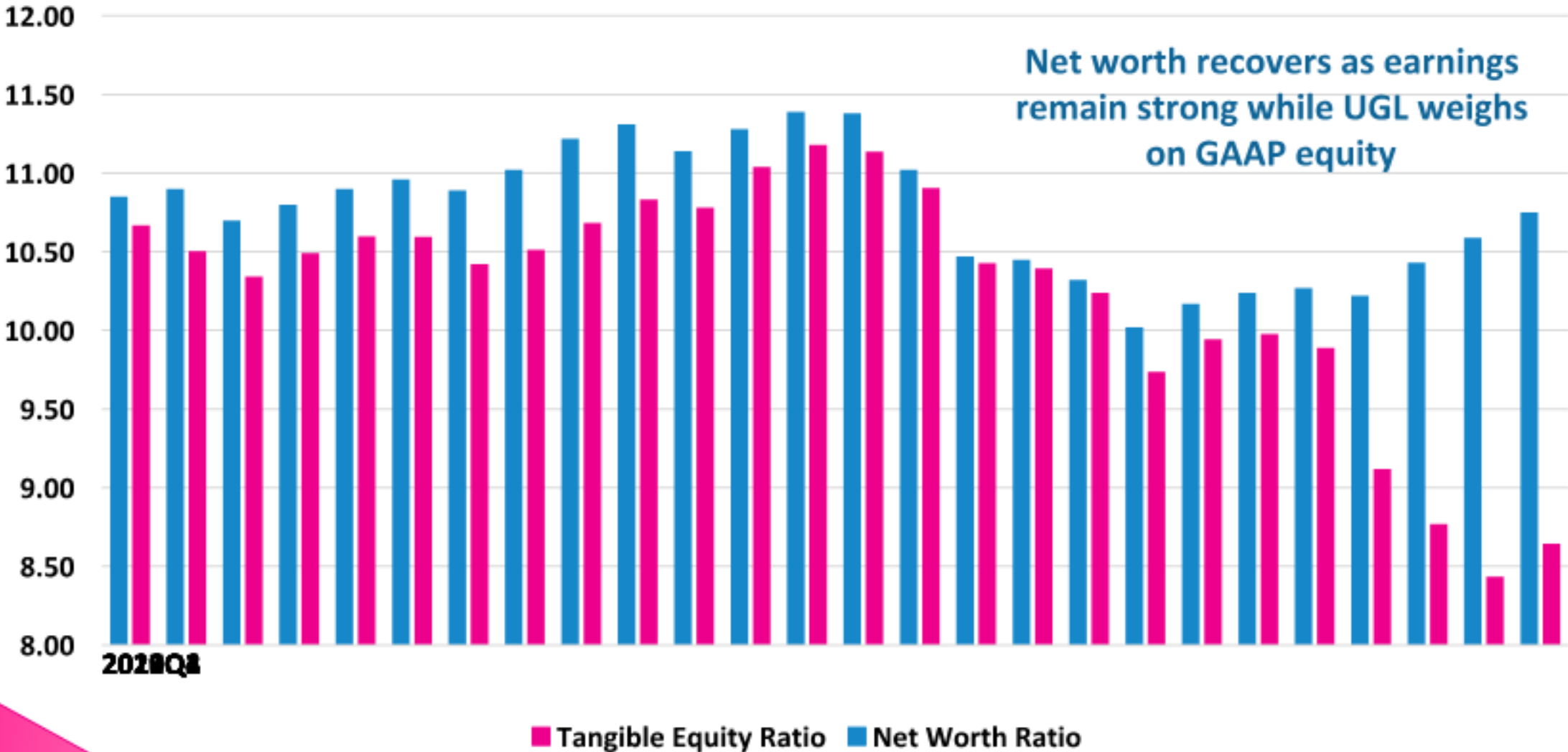
Capital Trends – CUs vs Banks



Source: S&P Global Market Intelligence; ALM First

Note: Bank population includes banks with total assets between \$1B and \$50B

CU Net Worth vs. Tangible Equity Ratio





Silicon Valley Bank from a Board and Management Perspective

**Tim Harrington, CPA & President
TEAM Resources**



Was SVB a Victim of a Bad Market?

“SVB’s failure is a textbook case of mismanagement.”

Michael Barr

Vice Chair for Supervision

Federal Reserve



Two of NCUA's "Red Flags" at SVB

1. Rapid Deposit Growth
2. High Level of Long-Term Assets to Total Assets

Two of NCUA “Red Flags” at SVB

1. Rapid Deposit Growth

Above market rates tend to attract less stable rate-sensitive shares. If the credit union then invests these sensitive deposits in longer-term assets (e.g., real-estate loans), it creates a mismatch of maturities for assets and liabilities that could further increase exposure to IRR.

1. Rapid Deposit Growth

Annual Deposit Growth Rate	2019	2020	2021	2022
Banking Industry	4%	17%	8%	-1%
Credit Unions	8%	18%	12%	5%
Silicon Valley Bank	41%	70%	79%	-8%
Total Assets	\$70BB			\$209BB

2. High Level of L-T Assets/Total Assets

“We are comfortable being able to put some of that money to work in longer duration” securities on our balance sheet.

Greg Becker

CEO of Silicon Valley Bank

in his 1Q 2021 earnings call

Two NCUA “Red Flags” at SVB

2. High level of long-term assets to total assets.

A high concentration of assets with maturities longer than three years will reduce the credit union's ability to react to changing interest rates and expose it to increased interest-rate risk.

What Can a Board and Management Team Watch?

1. Maintain Deposit Growth at a manageable pace
2. Watch Duration on Earning Assets (life of the asset)
3. Monitor projections of Capital at Risk and be prepared to restructure your Balance Sheet
4. Review Concentration Limits in IRR and ALM policies



SVB: The End of the Story

A communication perspective from (way) outside

Daniel Lally, Business Development & PR for
Strategic Communications
St. Gregory Group

Learning Objectives

- In this presentation we will discuss:
 - Communication timeline of SVB incident
 - What we knew then
 - What *might* have made a difference
 - What we know now

Disclaimers

1. I wasn't in any of the meetings described
2. I have no known personal or professional relationships with any of the principals
3. Incidents described are sourced from contemporaneous news reports

The Timeline

March 8: A Wednesday

- Initial Announcement via PRNewswire
 - Very technical language
 - Confusing central messaging
 - No context or explanation
 - Bottom line: taking a loss and raising capital

The Timeline

March 8: A Wednesday Gets Worse

- Zoom Call
 - SVB leadership discusses situation with stakeholders
 - Unscripted (and unfocused)
 - CEO asks depositors to “stay calm” and “not panic”
 - Takes no questions

The Timeline

SVB Financial Group (SIVB)

NasdaqGS · NasdaqGS Real Time Price. Currency in USD

Follow

Visitors trend 2W ↑ 10W ↑ 9M ↑

Quote Lookup

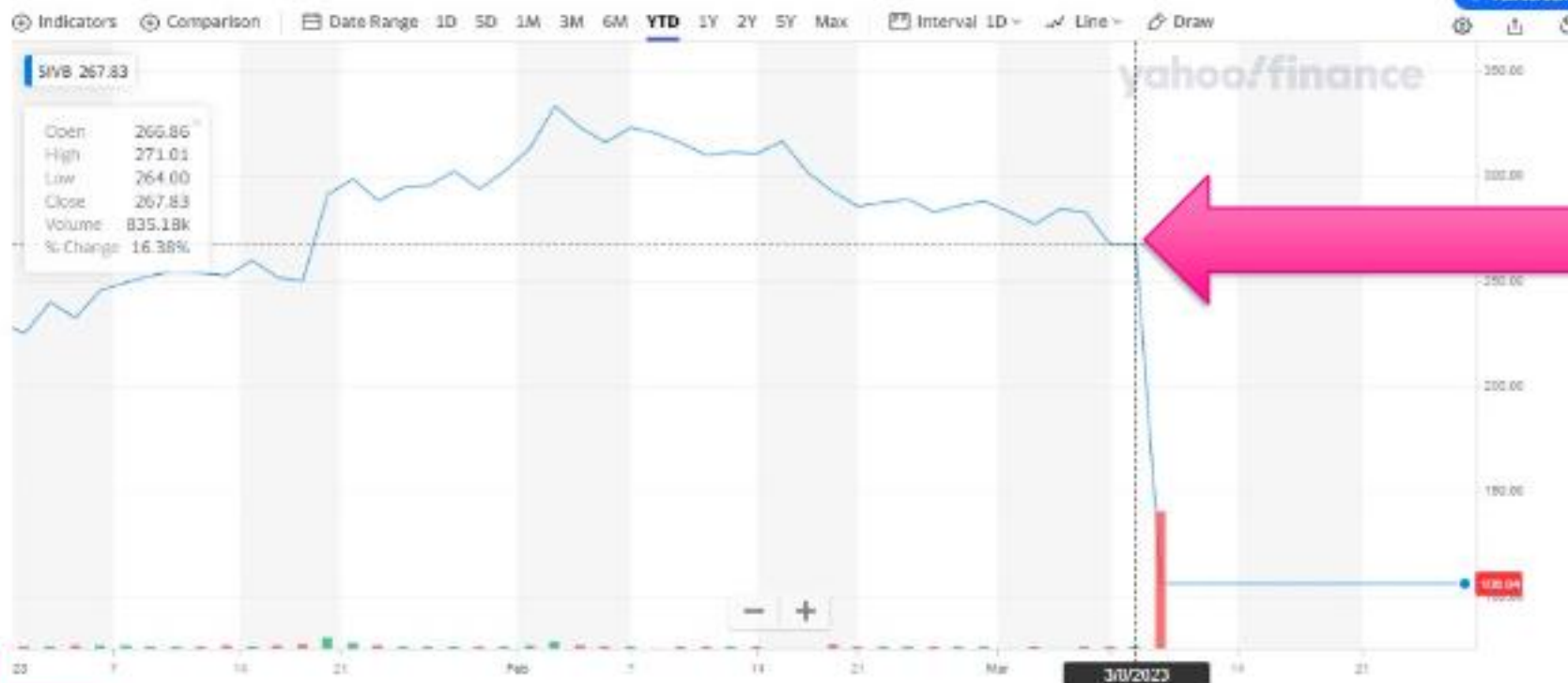


106.04 0.00 (0.00%)

As of March 9 05:00PM EDT. Market open.

Delisting: SIVB is delisted effective Mar. 28, 2023

Summary Company Insights **Chart** Conversations Statistics Historical Data Profile Financials Analysis Options Holders Sustainability



<https://tinyurl.com/33k3h2jw>

The Timeline

March 9: A Thursday

- Scared people do scared people things
 - SIVB loses 60 pct. in market value
 - Large withdrawals multiply
 - SVB maintains radio silence
 - Nature abhors a vacuum ...

The Timeline



Cassandra B.C.
@michaeljburry



It is possible today we found our Enron.

3:25 PM · 3/9/23 · **86.2K** Views

339 Retweets **101** Quotes **2,002** Likes

7:29 PM · Mar 9, 2023 · **313.3K** Views

<https://twitter.com/BurryArchive/status/1633988433961177088>

The Timeline

March 10: A Friday

- If enough people say a thing ...
 - More depositors withdraw more funds
 - Demand outstrips available cash
 - FDIC steps in and ...

- CURTAIN -

An Outside Take

Initial Communication

- Release was not enough
 - “convoluted”
 - No explanation or context
 - Did not inspire confidence
 - Failed to address stakeholder concerns

An Outside Take

The Zoom Call

- Loosely scripted statement
 - Was never a conversation
 - In public or in private
 - Action speaks louder
 - But words still matter

In the Beginning

Disciplines Matter

- Best plan possible may not have mattered
 - But it wouldn't have hurt

In the Beginning

The Best Time to Light a Fire

- Start with listening
- Build relationships
- How would you tell a 9-year-old?
- What if a human being said that?

In the Beginning

The Best Time to Light a Fire (cont.)

- Business is personal
 - Decisions are made by human beings
 - Emotional, irrational, conflicted human beings
- Know your stakeholders
 - Who they are, how they get information

Questions for our speakers...



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Co-founder & President
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Themes in Regulatory Priorities

Cyber Fraud

- Cyber event preparedness
key assumptions, especially non-maturity deposits
- Fraud detection, alert monitoring, and controls
-

Interest Rate Risk

- Overall inherent exposure
- Support/documentation of
key assumptions, especially non-maturity deposits
- Proactive strategies for the environment

Succession Planning

- Key staff succession
- Strategic viability
-

Liquidity Risk

- On balance sheet liquidity
- Contingent funding availability
- Stress testing and governance

Credit Risk

- Financial institution partnerships
- Assessment of opportunity and risk

Credit Risk

- Overall risk (balance sheet composition)
- Collection practices
- Portfolio monitoring

Thank you to our speakers...



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