The Daily Dish

The Fed Reports on Silicon Valley Bank

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Today the Federal Reserve is expected to release its report on the events leading to the failure of Silicon Valley Bank (SVB). This will be the first of any number of studies on the bank and there are a few things to look for.

The first is the scope of the report. Clearly there will be a timeline of events covered in the report. How comprehensive will that be? Will it include supervision over the prior two years, the decision to close SVB, and the events around the attempted sale and the use of the systemic risk exception for a bank not designated as systemically important? Or, does it limit itself in some way so that a complete accounting of the events is not possible?

The second is, what responsibility the Fed will take for the failure? Thus far, government officials have closed ranks around the “bad management” explanation of SVB’s demise. Certainly it is among the worst-managed banks ever. But will the Fed also take responsibility for what was clearly a supervisory failure? Not only did the regulator ignore its own internally generated warning reports, but all the classic signs of a company under stress were there. The percentage of insured deposits was extraordinarily high and a flashing warning light. How could this have taken anyone by surprise?

There is a second aspect of Fed responsibility. SVB’s circumstances were caused at least in part by macroeconomic factors. Rising interest rates and tightening credit as a result of the Fed’s own anti-inflation efforts largely kicked off this mess. To what extent does the Fed believe these risks are widespread in the broader banking sector, and what responsibility does the Fed take for creating them? Will this prompt any rethinking of the basic strategy of raising rates and shrinking the portfolio? Eakinomics thinks the Fed correctly believes it can manage the inflation fight and bank liquidity issues simultaneously using different tools. Will the report include this argument?

Does the Fed pin some of the responsibility on Congress? The Fed could attempt to pin blame on deregulation, particularly the 2018 Trump mid-size bank regulatory reform. Eakinomics thinks this is a lot of hooey, but it is easy to hide behind congressional errors. If so, how bold is the Fed going to be in proposing that Congress immediately step in to legislate a solution to this imaginary problem?

Finally, what will we learn about the modern banking environment? One of the few truly interesting aspects of this debacle was the Twitter-aided speed of the bank run. Banking is uniquely reliant on trust and investor confidence. To what extent does the regulator need to reconsider bank runs in the age of instantaneous information, correct or not?

It will be great to have something good to read this weekend.