
BANKS IN TURMOIL

The Ides of March 2023: Silicon Valley Bank and Credit Suisse

2023

That's Me

Corporate Finance Concepts
Christian Schopper
Second Edition

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You Never Really Know When The Avalanche Is Coming ...

... Until It Comes



☰ THE WALL STREET JOURNAL

Mar 10, 2023 at 10:41 am ET

SVB Financial Pulls Capital Raise, Explores Alternatives Including Possible Sale, Sources Say



Silicon Valley Bank's shares were halted after declining sharply. DAVID PAUL MORRIS/BLOOMBERG NEWS

☰ FINANCIAL TIMES myFT

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Now even its cornerstone investor is kicking Credit Suisse

More funding? "Absolutely not"



© AFP via Getty Images

With Ides of March Approaching ...



Last days of February 2023

- **SVB approached Goldman Sachs**
 - ... with clean bill of health for 2022 signed by KPMG
- **Needed to raise money to avoid funding squeeze**
 - **Soaring interest rates** had taken a heavy toll
 - **Deposits and the value of the bank's bond portfolio had fallen sharply**
 - Moody's Investors Service was preparing a downgrade

10 March 2023

- **SVB pulls share capital increase**



15 March 2023

- **“Absolutely not ... - The simplest reason is regulatory and statutory”**
 - Chairman Ammar Al Khudairy / **Saudi National Bank on further injections** if CS required additional liquidity
 - SNTIB in **deep loss** on its **9.9% CS stake** it had bought in October 2022
 - Citigroup: “SNTIB investors see the CS transaction as a huge **distraction for SNTIB's investment case ..**”
 - ... worrying that its status as a proxy for Saudi Vision 2030 reform was being diluted

The Status Quo



10 March 2023

- **Under control of the FDIC**
 - Federal Deposit Insurance Corp
- **SVB parent company** filed for bankruptcy / **Chapter 11**
 - Easing a sale of SVB's remaining assets: investment management and investment banking

26 March 2023

- **Much of loan and deposit portfolio acquired by First Citizens**



15 March

- **US\$ 50bn+ liquidity backstop** provided by the Swiss National Bank **not sufficient**
 - CS shares fell 30%, sparking a sell-off in European and US bank stocks
 - CS lost approximately US\$ 10bn deposits a day ...

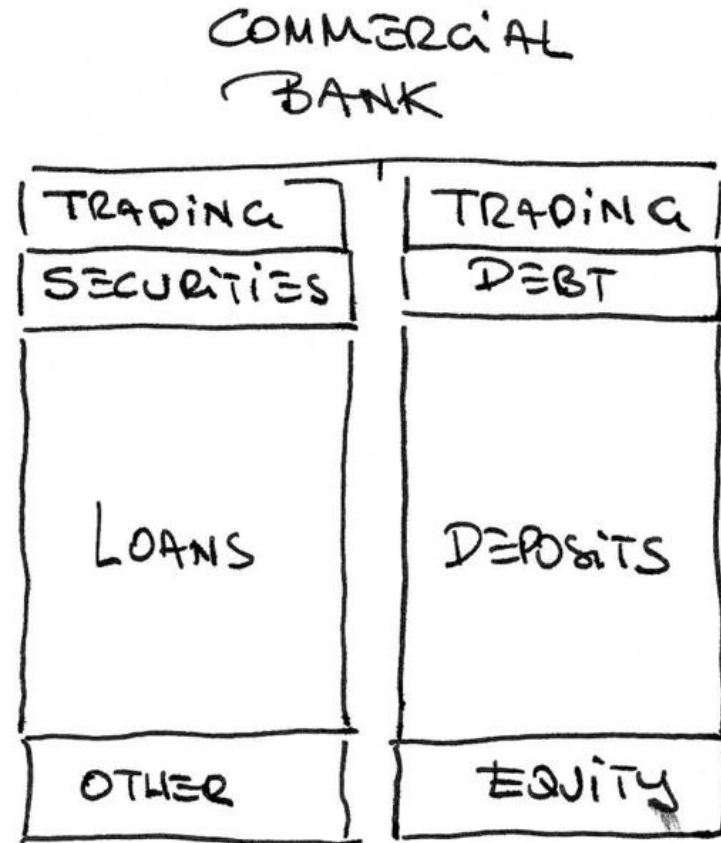
19 March 2023, late evening

- **CS "acquired" by UBS**
 - One of the biggest global systemically important financial institutions in Europe
 - Total assets: UBS US\$ 1.1tn, CS US\$ 575bn

Banks are Notoriously Difficult to Analyze, Leave Alone: To Run

Banks are highly delicate, fragile entities

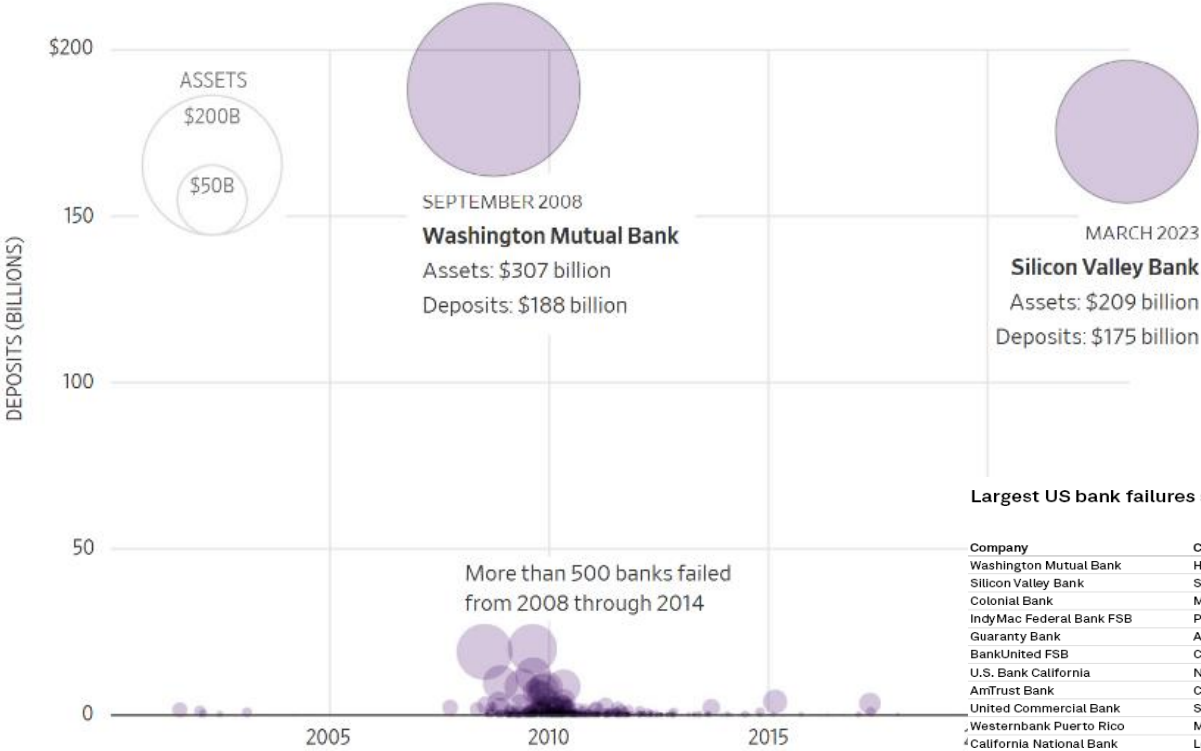
1. Institutions lend medium- / long-term, whilst the funding base (i.e. deposits held) is vastly short-term
 - A bank's balance sheet mirrors a massive **maturity transformation**
 - Ability to re-fund liabilities smoothly and on an ongoing basis is essential
2. Compared to any ordinary corporate, a **bank's balance sheet** is **extremely levered** ...
3. ... and regulated



Silicon Valley Bank

US Bank Failures

Bank failures, 2001-23



Note: Figures for assets and deposits are estimates.
Source: Federal Deposit Insurance Corp.

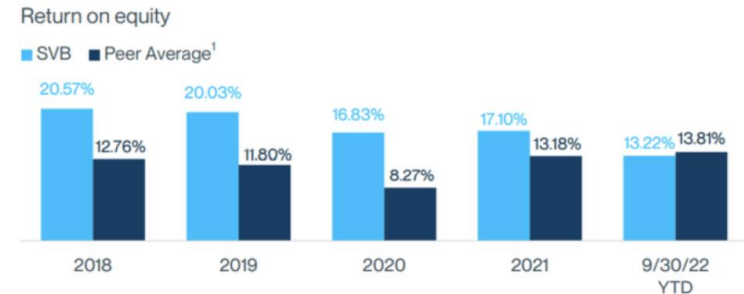
Largest US bank failures since 2008

Company	City, state	Date of failure	Year established	Total assets (\$B)	Total deposits (\$B)	Tangible assets/total assets (%)	equity/total assets (%)	Leverage ratio (%)
Washington Mutual Bank	Henderson, NV	09/25/08	1988	307.02	188.26	5.60	7.07	
Silicon Valley Bank	Santa Clara, CA	03/10/23	1983	209.03	175.38	7.27	7.96	
Colonial Bank	Montgomery, AL	08/14/09	1917	25.46	20.07	2.17	4.18	
IndyMac Federal Bank FSB	Pasadena, CA	07/11/08	1936	23.48	6.53	-19.66	-23.83	
Guaranty Bank	Austin, TX	08/21/09	1988	13.46	11.98	-5.20	-7.11	
BankUnited FSB	Coral Gables, FL	05/21/09	1984	13.11	8.78	-3.91	-3.24	
U.S. Bank California	Newport Beach, CA	11/21/08	1957	12.78	9.65	7.50	7.48	
AmTrust Bank	Cleveland, OH	12/04/09	1889	11.44	8.56	2.41	2.47	
United Commercial Bank	San Francisco, CA	11/06/09	1974	10.90	7.65	2.71	2.20	
Westernbank Puerto Rico	Mayaguez, PR	04/30/10	1958	10.80	8.42	3.49	3.44	
California National Bank	Los Angeles, CA	10/30/09	1998	7.78	6.15	3.29	0.06	
Corus Bank NA	Chicago, IL	09/11/09	1913	7.00	7.06	-2.31	-2.08	
First Federal Bank of California FSB	Santa Monica, CA	12/18/09	1929	6.14	4.54	4.25	4.25	
Doral Bank	San Juan, PR	02/27/15	1981	5.90	4.10	7.18	2.23	
R-G Premier Bank of Puerto Rico	San Juan, PR	04/30/10	1983	5.68	4.22	3.86	3.69	
Group median						3.29	2.47	
Median for failures since 2008						1.27	1.18	

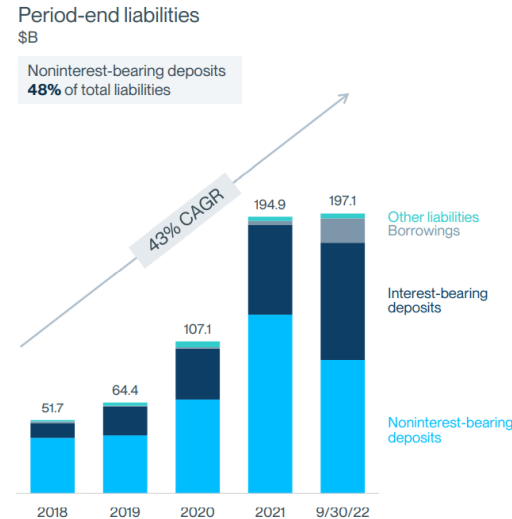
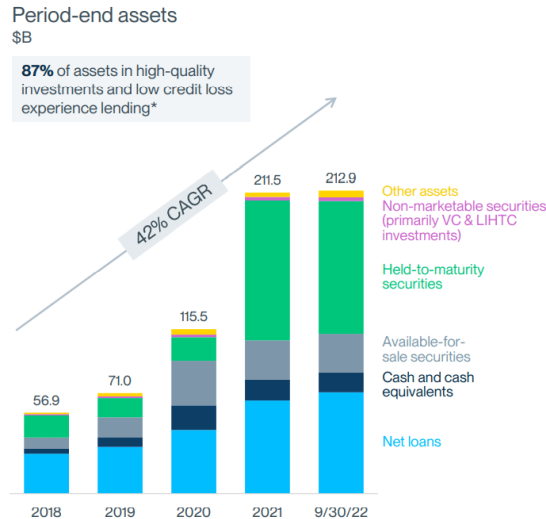
Data compiled Mar. 10, 2023.
Analysis limited to commercial bank, savings bank, and savings and loan association failures in the U.S. between Jan. 1, 2008, and Mar. 10, 2023.
Financial data based on most recent regulatory filings before failure.
Sources: S&P Global Market Intelligence; Federal Deposit Insurance Corp.
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Actually, It's Looking Good ...

- 18th largest US bank
- Serving nearly half of US-American VC-backed technology and life-sciences companies as clients



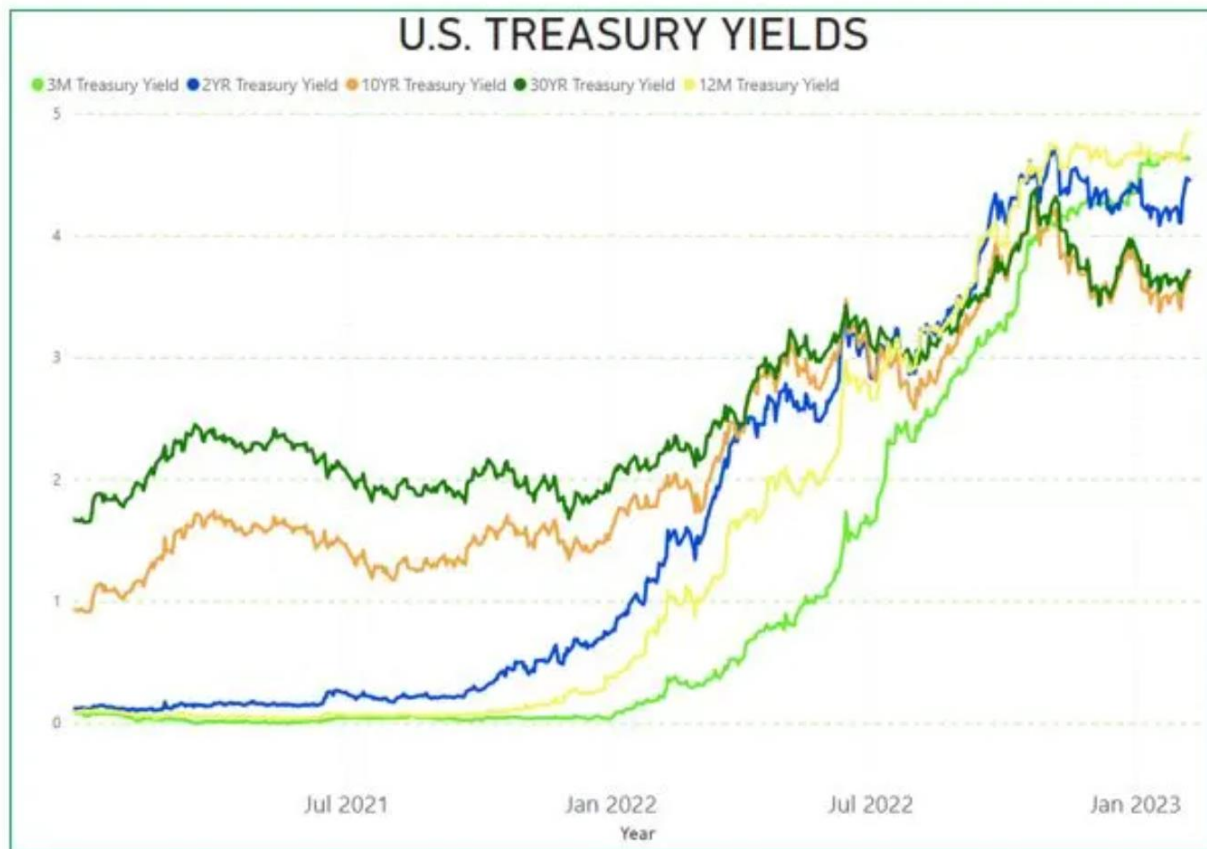
SVB ROE's by Year vs Comps (Q3 SVB Presentation)



* Based on cash, fixed income investment portfolio and Global Fund Banking and Private Bank loan classes of financing receivables as of September 30, 2022.

Q3 2022 FINANCIAL HIGHLIGHTS

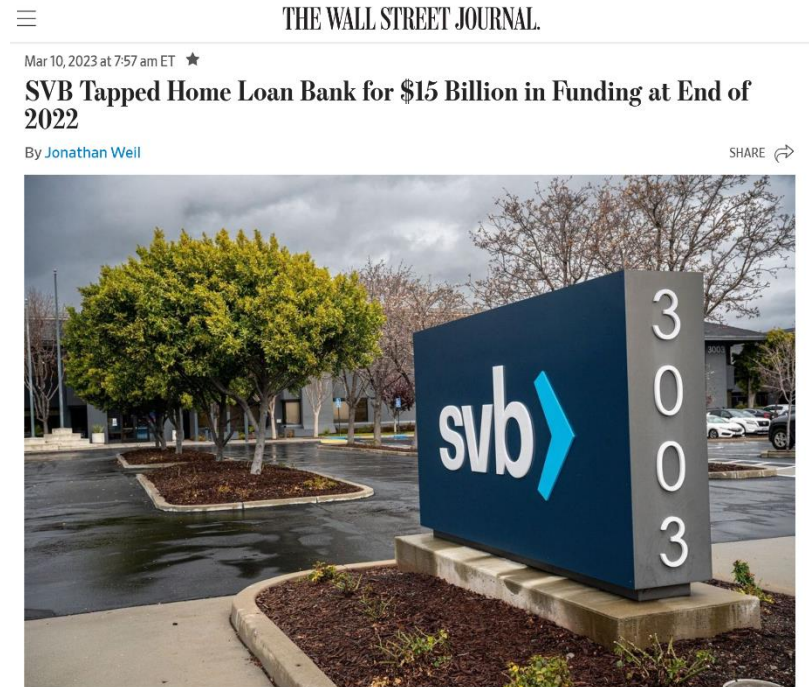
... but the Environment is Changing - and Fast



Source: FCIS Research and Analytics

Latest by YE 2022, Liquidity Becomes an Issue

- **US\$ 15bn of loans outstanding from the Federal Home Loan Bank of San Francisco**
 - Had none a year earlier
 - As collateral SVB pledged almost three times what it borrowed to back
 - **FHLBs**, were founded to support housing finance during the Great Depression
 - Today, they direct cash into the banking system, using their implicit government backing to borrow money cheaply
 - **FHLB loans** appear to have **coincided with a US\$ 25bn, or 13%, decline in deposits** during the final three quarters of 2022



Signage outside Silicon Valley Bank headquarters in Santa Clara, California. DAVID PAUL MORRIS/BLOOMBERG NEWS

SVB Balance Sheet (YE 2022)

SVB FINANCIAL GROUP AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS		
(Dollars in millions, except par value and share data)	December 31,	
	2022	2021
Assets		
Cash and cash equivalents	\$ 13,803	\$ 14,586
Available-for-sale securities, at fair value (cost of \$28,602 and \$27,370, respectively, including \$530 and \$61 pledged as collateral, respectively)	26,069	27,221
Held-to-maturity securities, at amortized cost and net of allowance for credit losses of \$6 and \$7 (fair value of \$76,169 and \$97,227, respectively)	91,321	98,195
Non-marketable and other equity securities	2,664	2,543
Total investment securities	120,054	127,959
Loans, amortized cost	74,250	66,276
Allowance for credit losses: loans	(636)	(422)
Net loans	73,614	65,854
Premises and equipment, net of accumulated depreciation and amortization	394	270
Goodwill	375	375
Other intangible assets, net	136	160
Lease right-of-use assets	335	313
Accrued interest receivable and other assets	3,082	1,791
Total assets	\$ 211,793	\$ 211,308
Liabilities and total equity		
Liabilities:		
Noninterest-bearing demand deposits	\$ 80,753	\$ 125,851
Interest-bearing deposits	92,356	63,352
Total deposits	173,109	189,203
Short-term borrowings	13,565	71
Lease liabilities	413	388
Other liabilities	3,041	2,467
Long-term debt	5,370	2,570
Total liabilities	195,498	194,699
Commitments and contingencies (Note 21 and Note 26)		
SVBFG stockholders' equity:		
Preferred stock, \$0.001 par value, 20,000,000 shares authorized; 383,500 and 383,500 shares issued and outstanding, respectively	3,646	3,646
Common stock, \$0.001 par value, 150,000,000 shares authorized; 59,171,883 and 58,748,469 shares issued and outstanding, respectively	—	—
Additional paid-in capital	5,318	5,157
Retained earnings	8,951	7,442
Accumulated other comprehensive income (loss)	(1,911)	(9)
Total SVBFG stockholders' equity	16,004	16,236
Noncontrolling interests	291	373
Total equity	16,295	16,609
Total liabilities and total equity	\$ 211,793	\$ 211,308

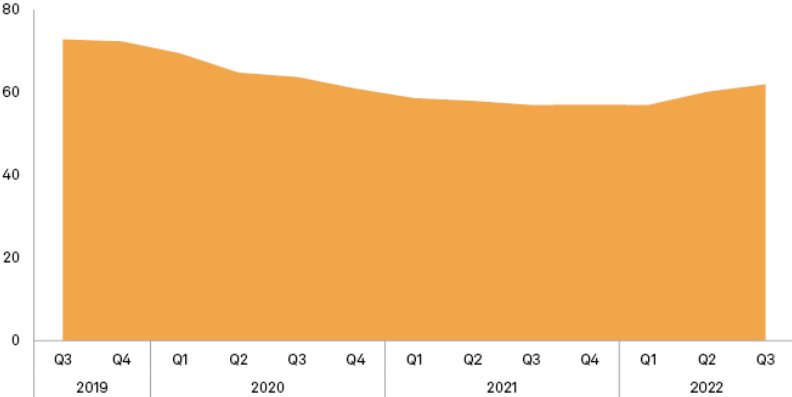
SVB Balance Sheet (YE 2022) - Key Figures

COMMERCIAL
BANK

120	TRADING SECURITIES	TRADING DEBT	
74	LOANS	DEPOSITS	173
	OTHER	EQUITY	16
211	Total Assets and Liabilities		211

SVB Balance Sheet (YE 2022) - US Bank Loans-Deposit Ratios

Loans-to-deposits ratio since Q3 2019 (%)




Data compiled Nov. 22, 2022.
 Analysis includes U.S. commercial banks, savings banks, and savings and loan associations. Nondepository trusts and companies with a foreign banking organization charter are excluded.
 Data based on regulatory filings.
 Source: S&P Global Market Intelligence.
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COMMERCIAL BANK

120	TRADING SECURITIES	TRADING DEBT	
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211	Total Assets and Liabilities		211

SVB Balance Sheet (YE 2022) – A January Tweet Seems Spot On ...

Raging Capital Ventures 
 @RagingVentures · Follow

Replying to @RagingVentures

\$SIVB's HTM securities had mark-to-market losses as of Q3 of \$15.9 b...compared to just \$11.5 b of tangible common equity!!

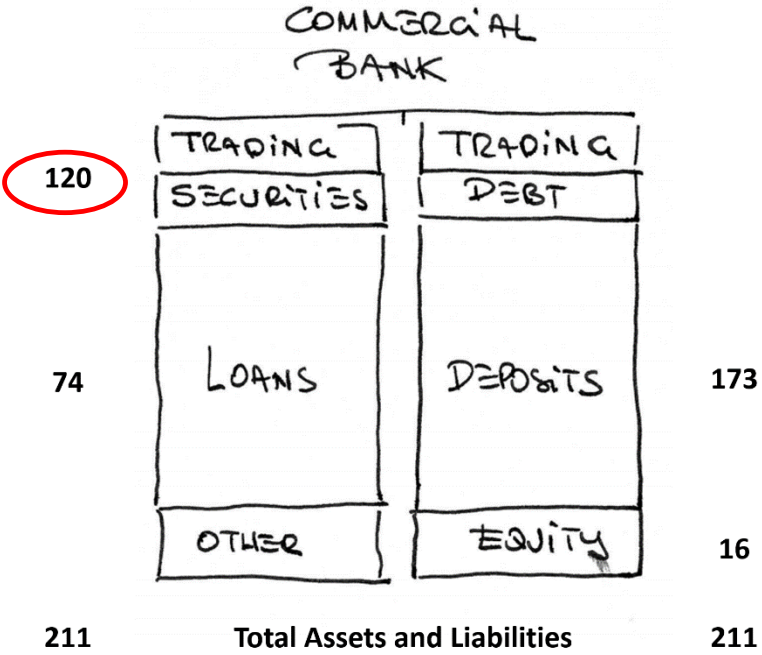
Luckily, regulators do not force \$SIVB to mark HTM securities to market. But the bank would be functionally underwater if it were liquidated today. 5/10

	September 30, 2022		Fair Value
	Unrealized Gains	Unrealized Losses	
486	\$	—	\$ 433
59,200	—	(10,017)	49,183
10,741	—	(1,813)	8,928
83	—	(1)	82
14,644	—	(2,304)	12,340
7,429	—	(1,612)	5,817
709	—	(122)	587
93,292	\$	—	\$ 77,370

10:38 PM · Jan 18, 2023

756 Reply Share

Read 8 replies



SVB Balance Sheet (YE 2022) – Securities Classifications

Available for Sale

(Dollars in millions)	December 31, 2022					
	Less than 12 months		12 months or longer		Total	
	Fair Value of Investments	Unrealized Losses	Fair Value of Investments	Unrealized Losses	Fair Value of Investments	Unrealized Losses
AFS securities, at fair value:						
U.S. Treasury securities	\$ 11,946	\$ (717)	\$ 4,189	\$ (354)	\$ 16,135	\$ (1,071)
U.S. agency debentures	—	—	101	(19)	101	(19)
Foreign government debt securities	1,088	(121)	—	—	1,088	(121)
Residential MBS:						
Agency-issued MBS	1,744	(203)	4,859	(895)	6,603	(1,098)
Agency-issued CMO —fixed rate	136	(11)	542	(73)	678	(84)
Agency-issued CMBS	810	(57)	653	(83)	1,463	(140)
Total AFS securities (1)	\$ 15,724	\$ (1,109)	\$ 10,344	\$ (1,424)	\$ 26,068	\$ (2,533)

- (1) As of December 31, 2022, we identified a total of 810 investments that were in unrealized loss positions with 346 investments in an unrealized loss position for a period of time greater than 12 months. Based on our analysis of the securities in an unrealized loss position as of December 31, 2022, the decline in value is unrelated to credit loss and is related to changes in market interest rates since purchase, and therefore, changes in value for securities are included in other comprehensive income. Market valuations and credit loss analyses on assets in the AFS securities portfolio are reviewed and monitored on a quarterly basis. As of December 31, 2022, we do not intend to sell any of our securities in an unrealized loss position prior to recovery of our amortized cost basis, and it is more likely than not that we will not be required to sell any of our securities prior to recovery of our amortized cost basis. None of the investments in our AFS securities portfolio were past due as of December 31, 2022.

Held to Maturity

(Dollars in millions)	December 31, 2022					
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value	ACL (2)	Net Carry Value
HTM securities, at cost:						
U.S. agency debentures (1)	\$ 486	\$ —	\$ (52)	\$ 434	\$ —	\$ 486
Residential MBS:						
Agency-issued MBS	57,705	—	(9,349)	48,356	—	57,705
Agency-issued CMO—fixed rate	10,461	—	(1,885)	8,576	—	10,461
Agency-issued CMO—variable rate	79	—	(2)	77	—	79
Agency-issued CMBS	14,471	—	(2,494)	11,977	—	14,471
Municipal bonds and notes	7,417	2	(1,269)	6,150	1	7,416
Corporate bonds	708	—	(109)	599	5	703
Total HTM securities	\$ 91,327	\$ 2	\$ (15,160)	\$ 76,169	\$ 6	\$ 91,321

- (1) Consists of pools of Small Business Investment Company debentures issued and guaranteed by the SBA, an independent agency of the United States.
(2) Refer to Note 2—“Summary of Significant Accounting Policies” for more information on our credit loss methodology.

SVB Balance Sheet (YE 2022) – Securities „Available for Sale“

Available for Sale

(Dollars in millions)	December 31, 2022					
	Less than 12 months		12 months or longer		Total	
	Fair Value of Investments	Unrealized Losses	Fair Value of Investments	Unrealized Losses	Fair Value of Investments	Unrealized Losses
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- AFS
 - US\$ 26,1bn - Fair Market Value
 - US\$ 28,6bn - Cost
 - US\$ 2,5bn - Loss
 - By 8 March sold off
- Accounting Rules
 - AfS are **marked to market**, but **paper losses are excluded from earnings** - although count in equity

SVB Balance Sheet (YE 2022) – Securities „Held to Maturity“

Held to Maturity

(Dollars in millions)	December 31, 2022					
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- HTM

- US\$ 76,2bn - Fair Market Value
- US\$ 91,3bn - Cost
- US\$ 15,1bn - Loss (vs US\$ 16.3 equity)
- Foremost very-long-term, agency-guaranteed mortgage-backed bonds with basically no risk of default

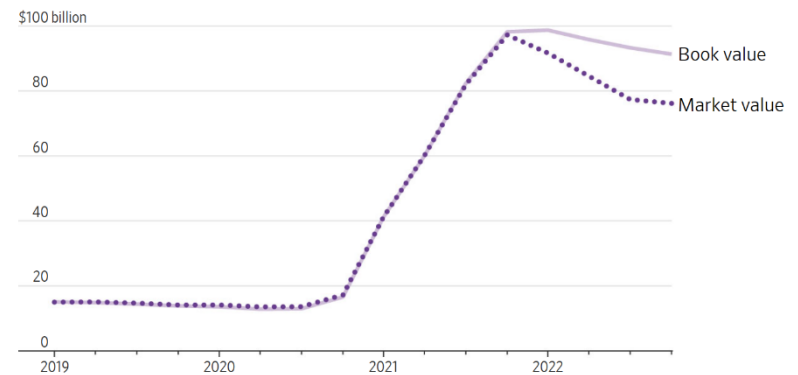
- Accounting Rules

- HTM securities allow a bank to **exclude paper losses** on those holdings **from both its earnings and equity**

Excursion: Would Have Hedging Securities “Held to Maturity” Helped?

- HTM securities **insulate a bank from short-term price volatility**
 - Also, in case of SVB, **holding Treasuries and MBS** required holding less capital because **deemed risk-free ...**
 - ... **leaving less buffer** when rates rise, though
- **When hedging a HTM portfolio, the value of the hedge would fluctuate with the market ...**
 - ... leaving the HTM portfolio at par
 - If rates fall, hedge loses money ...
 - ... but bank can shift bonds from HTM to AfS and sell them at higher price
 - Hence: **Directional bet on interest**
- Big commercial banks often hedge a bit of the interest rate risk, ...
 - ... just in case
- In general, though, banks hold shorter-term bonds to minimise interest rate sensitivity
- Since 2018, **SVB actually added a lot of duration** by piling into 30-year MBS ...

Bonds Silicon Valley Bank said it would hold until they matured



Source: Federal Financial Institutions Examination Council

SVB Balance Sheet (YE 2022) – Those Uninsured Deposits ...

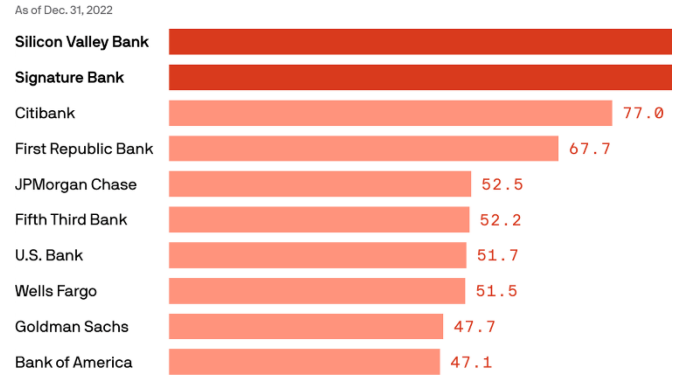
COMMERCIAL BANK

	TRADING SECURITIES	TRADING DEBT	
120			
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74			
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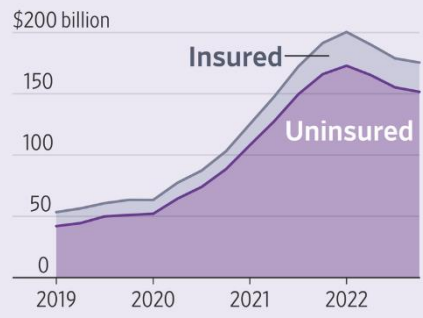
Deposits

- US\$ 92bn interest-bearing
- US\$ 81bn non interest-bearing

Percentage of domestic deposits that were uninsured



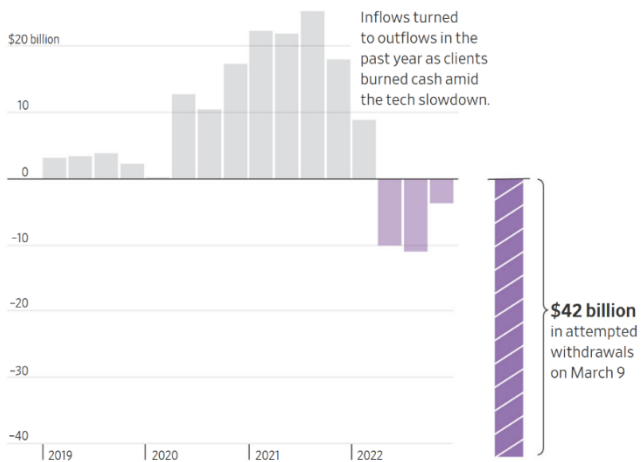
Silicon Valley Bank's deposits



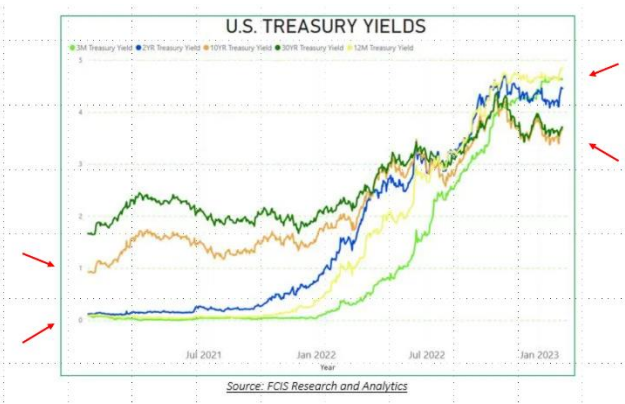
Reality Kicking In: „Normalizing“ Interest Rates

- Cheap funding is drying up ...
- ... and **SVB’s customers withdraw deposits** to keep business alive ...
- ... with **non-interest-bearing deposits falling dramatically**

SVB Financial deposits, quarterly net change



Sources: company filings (quarterly); California regulators (March 9)



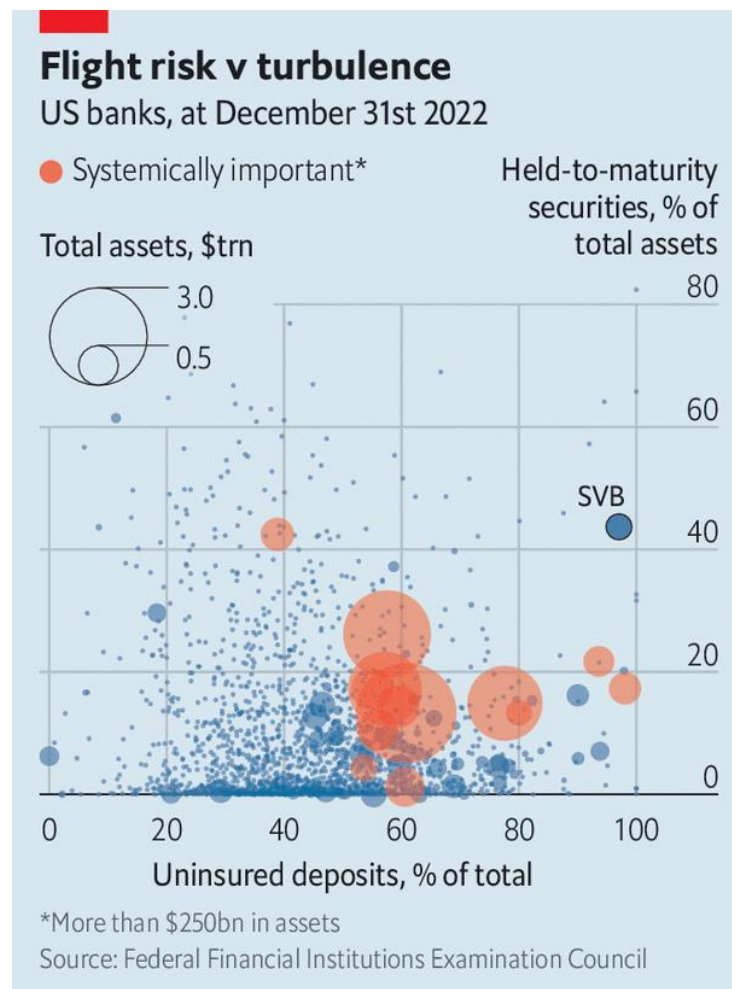
QoQ period-end total client funds ("TCF") by client activity (management's approximation)² \$B



The Toxic Mix of SVB

“... Unrealized losses weaken a bank’s future ability to meet unexpected liquidity needs.”

Martin Gruenberg , FDIC Chairman, in a March 6 speech



The Economist

Bank Runs 1920s vs 2023



The Goldman Sachs Plan

The SVB Problem

- SVB was **paying up to stop depositors from leaving ...**
- ... and was stuck **earning a pittance on low-risk bonds** bought in low-rate times

The Goldman Solution – Part 1

- SVB would **sell (most of) those bonds ...**
- ... and (i) **raise cash**; and (ii) **buy new bonds that paid more**

The Downside of the Goldman Solution – Part 1

- SVB would have to **realize a big loss**

The Goldman Solution – Part 2

- SVB would have to **raise equity**

10 Days To Hell

Late February 2023

- **SVB intended an accelerated private stock placement, ...**
 - Quietly lining up investors to buy a set number of shares at a set price
- ... not least as **Moody's prepared to downgrade SVB**
- ... **Goldman, however, pitched a US\$ 2,25bn hybrid public-private share sale**
 - Also offer the public an opportunity to buy shares at the same price

5 March 2023

- One of the intended anchor investors, **Warburg, dropped out**
 - **Needed more time** to evaluate the deal than SVB was willing to give
 - Didn't want to participate in an offering with a public component
- In parallel, on Goldman's trading desk, another deal was coming together
 - **Seeking a buyer for SVB's US\$ 21bn AfS portfolio**
 - Eventually, though: The buyer would be Goldman ...

10 Days To Hell (cont'd)

7 March 2023

- Another anchor investor, **General Atlantic**, agreed to acquire up **US\$ 500m** in the **stock** sale
 - But **time was running out for the remaining US\$ 1,75bn**
 - And, SVB seemed reluctant to share the information investors needed
- Goldman continued to insist the **only option** was a **public share offering anchored by General Atlantic**
 - SVB executives signed off

8 March 2023

- **Goldman completed the purchase of the SVB AfS securities portfolio** at a discount
 - After the market closed, **SVB announced** that it had **realized a US\$ 1,8bn loss** on the sale ...
 - ... **without disclosing the buyer**, ...
 - ...and said it would sell shares to raise capital

10 Days To Hell (cont'd)

8 March 2023

- **SVB hired** deal-advisory firm **Centerview Partners to explore a plan B**
 - ... just prior the launch of its share sale ...
- Goldman still confident the share sale would come together ...
 - **SVB's stock fell** (8% in aftermarket), **not as steep** as feared ...
 - ... and appetite for SVB share offer seemed reasonably good
- The **mood shifted**, though, **when Silvergate Capital** (total assets ca US\$ 11,3bn) **announced** it was **shutting down** following a run on deposits
- **A one-notch Moody's downgrade, less severe than feared**, landed at around 20.00
 - Senior unsecured long term issuer rating from A3 to Baa1

9 March 2023

- When the market opened, **SVB shares tanked, prompting customers to pull their deposits ...**

10 Days To Hell (cont'd)

9 March 2023

- **By the time SVB closed for business, depositors had attempted to withdraw US\$ 42bn**

“The best place to be in a bank run is first out the door ...”

An SVB customer

10 March 2023

- **FDIC seized SVB** prior opening

COMMERCIAL BANK

120	TRADING SECURITIES	TRADING DEBT	
74	LOANS	DEPOSITS	173
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Market Stabilisation Measures – New Bank Term Funding Program (BTFP)

13 March 2023

1. FDIC stepped up to **guarantee all deposits at SVB (incl. uninsured funds)**
 2. Federal Reserve **unveiled a new BTFP**
 - Designed for banks to be able to **borrow funds backed by government securities** to meet withdrawal demands from deposits
- Tenor: **“This is Not a Bail-Out”**, only depositors are protected
 - ... whilst SVB shareholders and unsecured creditors are not
 - BTFP
 - Loans of up to one year in length to banks and other eligible depository institutions ...
 - ... pledging U.S. Treasuries, agency debt and mortgage-backed securities, and other qualifying assets as collateral
 - **These assets will be valued at par**
 - With approval of the Treasury Secretary, the Department of the Treasury will make available up to US\$ 25bn from the Exchange Stabilization Fund as a backstop for the BTFP
 - The Federal Reserve does not anticipate that it will be necessary to draw on these backstop funds

Selected Voices ... - How Could This Happen? And Where Was the Regulator?

“Rapid growth should always be at least a yellow flag for supervisors ..”

“Nearly 90% of SVB’s deposits were uninsured ..”

“A US\$ 200bn bank should not fail because of liquidity ..”

“Imagine: The banking industry as a whole had some US\$ 620bn in unrealized losses on securities at the end of 2022 ...”

- The Federal Reserve was the primary federal regulator for SVB

Excursion: On Rules and Regulations – SVB and the Dodd-Frank Act

- **Enacted in July 2010**, the Dodd-Frank Act overhauled the entire financial regulation in the US
- **Under President Trump**, part of Dodd-Frank were **rolled back**, easing oversight of small and regional lenders
 - A measure in May 2018 **lifted the threshold for being considered “systemically important”** — a label imposing **requirements including annual stress testing** — to US\$ 250bn in assets, up from US\$ 50bn
 - SVB had just crested US\$ 50bn at the time. By early 2022, it had swelled to US\$ 220bn, among the top 20 US banks
- In 2015, SVB CEO Greg Becker urged the government to increase the threshold, arguing it would otherwise lead to higher costs for customers and “stifle our ability to provide credit to our clients ...”
 - With a core business of traditional banking — taking deposits and lending to growing companies — SVB doesn’t pose systemic risks, he said

Excursion: SVB Losses Embolden Calls for US Accounting Rule Reform

- Advocates of “fair value” accounting are urging the FASB to force banks to recognise **HTM-related unrealised losses** ...
 - ... even when management insists they will never have to be sold
 - Could have forced SVB to take action to shore up its finances before it was too late
- Not just an academic debate about which approach would paint the “correct” picture of what an asset is worth, ...
- ... as **accounting rules affect banks’ behavior** ...



Accountancy [+ Add to myFT](#)

Silicon Valley Bank losses embolden calls for US accounting rule reform

‘Fair value’ approach would have made SVB’s losses on bond portfolio obvious to investors earlier, say advocates

svb Silicon Valley Bank

Before its collapse, Silicon Valley Bank had parked \$91bn in a portfolio of bonds whose market value had fallen to \$76bn because of rising interest rates © Reuters

As the Story Goes On ...

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Silicon Valley Bank + Add to myFT

Executive pay at Silicon Valley Bank soared after big bet on riskier assets

Bonuses jumped when wager on long-dated bonds boosted lender's returns



Greg Becker's cash bonus peaked at \$3mn in 2021, more than double the amount he received four years earlier © FT montage/Bloomberg

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Opinion **The Top Line**

Time to ask what the directors were doing at these failed banks

The fragility of financial institutions suggests serious lapses in corporate governance in banking and beyond



ANDREW EDGECLIFFE-JOHNSON + Add to myFT



© Brendan McDermid/Reuters

... With a (Sort Of) Ending

- The purchase **includes** US\$ 119bn in **deposits and** about US\$ 72bn of SVB's **loans** at a discount of \$16.5 billion
 - Some US\$ 90bn of SVB's securities will remain in receivership.
- The **FDIC agreed to share any of** First Citizens' **losses or potential gains on SVB's commercial loans**
 - Overall, the FDIC estimated the failure of SVB will cost a federal insurance fund it oversees about US\$ 20bn, or roughly 10% of the bank's assets before its failure

THE WALL STREET JOURNAL.

MARKETS

First Citizens Acquires Much of Failed Silicon Valley Bank

Deal with federal regulators will make Raleigh-based firm one of the top 25 U.S. banks



Silicon Valley Bank's headquarters in Santa Clara, Calif.

PHOTO: PRESTON GANNAWAY FOR THE WALL STREET JOURNAL

Selected Considerations for Bank Management

The Business Model of Banks

- A bank generally pays (relatively lower) on interest deposits ...
- ... to reinvest those in financial products with a higher rate of return (loans, equities, fixed income products)
 - **SVB had received enormous deposits** during the last years (i.e. run-up in VC funding through the pandemic) which it could not loan out fast enough
 - **Instead of making** (risky, higher-yielding) **loans, SVB decided to invest in fixed-income products** (e.g. long-dated, risk-free, low-yielding US government bonds)
 - In an environment of **rising interest rates**, the **price of low-yielding fixed income products declined**, whilst funding costs increased
 - Note: Besides SVB reported virtually **no interest rate hedges** on its bond portfolio

In Banking, Diversification is Key

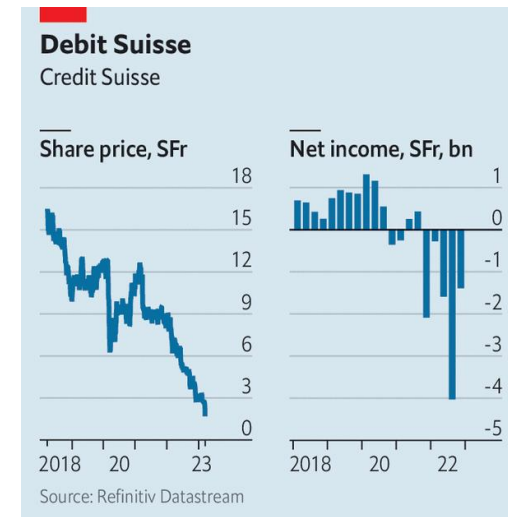
- SVB counted nearly half of the country's VC-backed technology and life-sciences companies as clients

And, Finally: **In Banking, Trust is Everything**

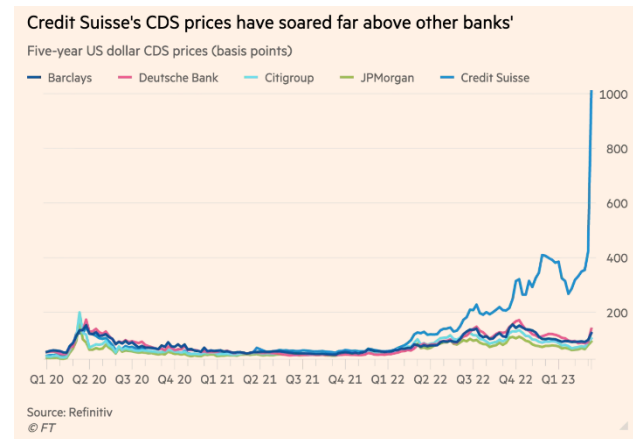
Credit Suisse

Who Is CS?

- CS was a **global investment bank** and financial services firm founded and based in Switzerland
 - #155 world-wide, global "bulge bracket" firm
 - Providing services in investment banking, private banking, asset management, and shared services
- CS was one of the **least affected banks during the global financial crisis**
 - Afterwards it began **shrinking its investment business ...**
 - Executing layoffs and cutting costs
 - ... **accompanied by multiple international investigations for tax avoidance**
 - Culminating in a guilty plea and fines of US\$ 2,6bn in 2008 - 2012



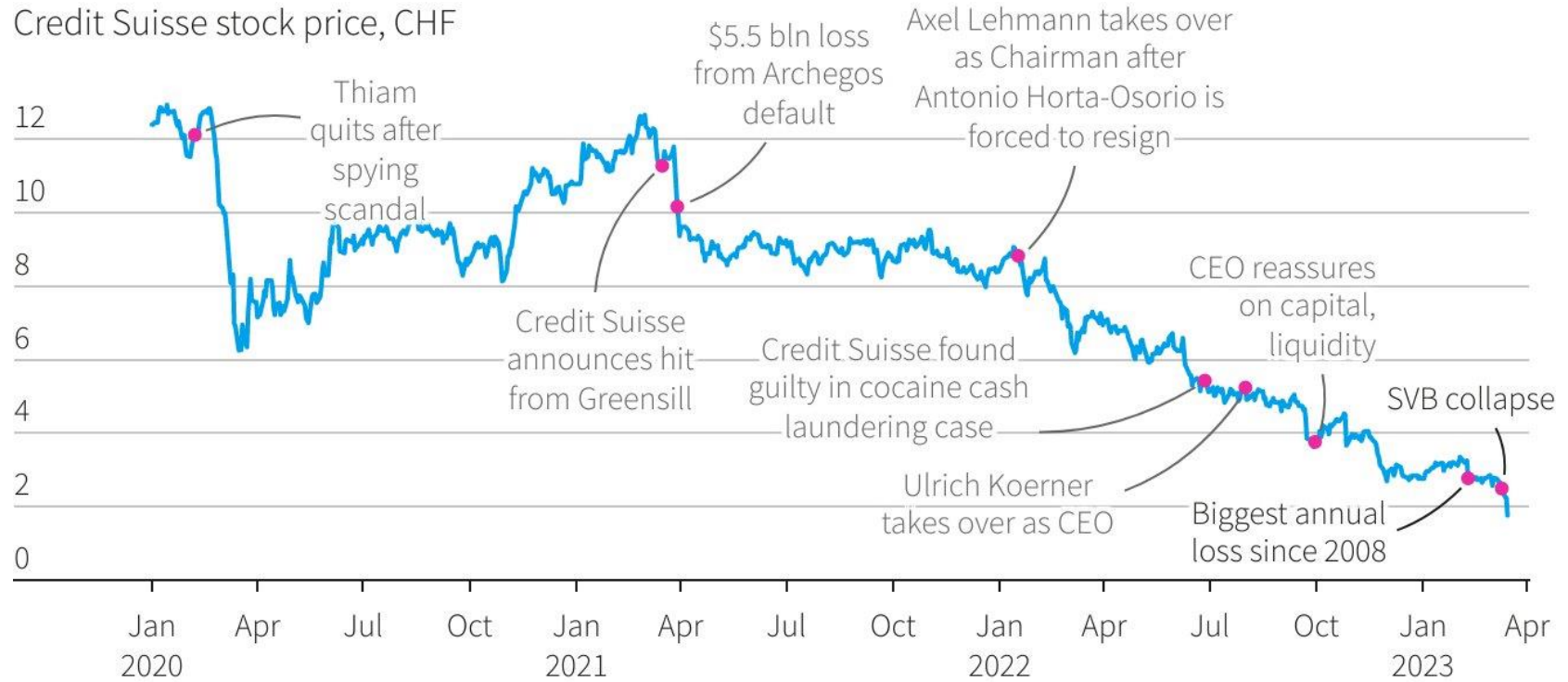
The Economist



A Troubled Recent History

Credit Suisse goes off piste

Credit Suisse stock price, CHF



Note: March 15, 2023 price as at 1054 GMT

Source: Refinitiv Datastream | Reuters, March 15, 2023 | By Vincent Flasseur

Spying Affair

- Breakdown in the relationship between CS CEO Thiam and Iqbal Khan, who ran CS's WM division
 - Swiss prosecutors are investigating an alleged **physical confrontation** between Mr Khan and three men hired by CS to follow him after he resigned in July to move to arch-rival UBS
 - ... leading to an angry altercation in downtown Zurich
 - The unedifying episode has raised **questions over the judgment of Mr Thiam**, who had an acrimonious relationship with Mr Khan, in part because of a string of neighbourly disputes concerning residences they each own in Zurich



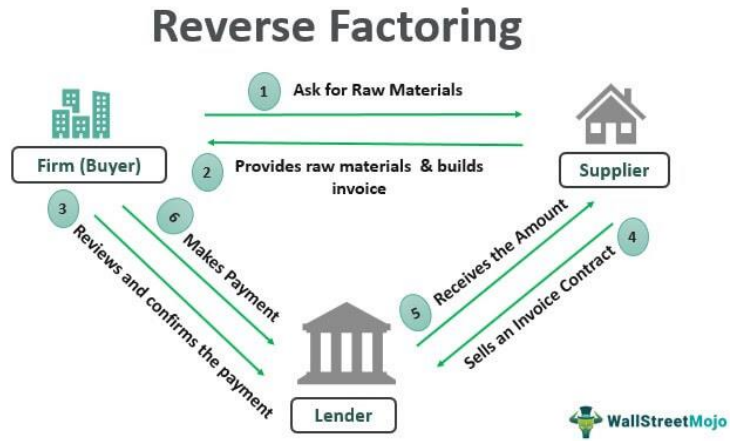
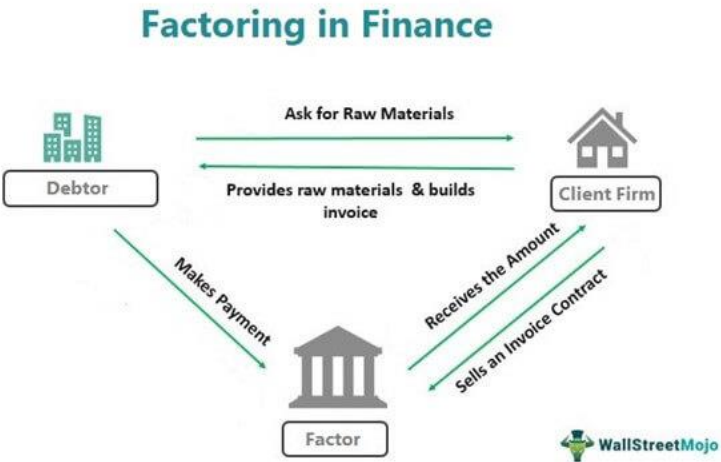
Greensill Affair

- Greensill Capital was a financial services company **focused on supply chain financing**
 - **Insolvency in March 2021**
 - 2011: Founded by Lex Greensill
 - 2018: General Atlantic (US\$ 250m)
 - 2019: Softbank / **Vision Fund** (US\$ 800m)
 - 2020: Pursuit of other investors to raise US\$ 500 – 600m aiming for an IPO within two years
- To fund its activities, Greensill **relied on loans ...**
- **... provided by supply-chain investment funds managed by CS**
 - To manage its risk, Greensill took out credit insurance with Tokio Marine
- July 2020: **Tokio Marine** insuring US\$ 4,6bn of Greensill working capital, announced that it would **stop providing coverage**
 - One of its employees had exceeded risk limits (fraud claim)
- March 2021: **CS froze US\$ 10bn in funds** invested in Greensill's financial products, held by its supply-chain investment funds
 - Increasing concerns with Greensill's large **exposure to** companies to steel magnate **Sanjeev Gupta**
- Later CS estimated that **investors** in its supply-chain funds could sustain **losses of up to US\$ 3bn ...**
 - ... having been **marketed as low-risk**

Excursion: Factoring vs Supply Chain Financing / Reverse Factoring

- In traditional factoring, a firm will sell the invoices it has issued to clients to a third party (Greensill)
- The third party then collects the money owed from those clients

- In reverse factoring, a third party (Greensill) pays debts owed by a company to its suppliers at a slight discount, but much more quickly than the original company would have
- The third party later receives payment from the company



Archegos Affair

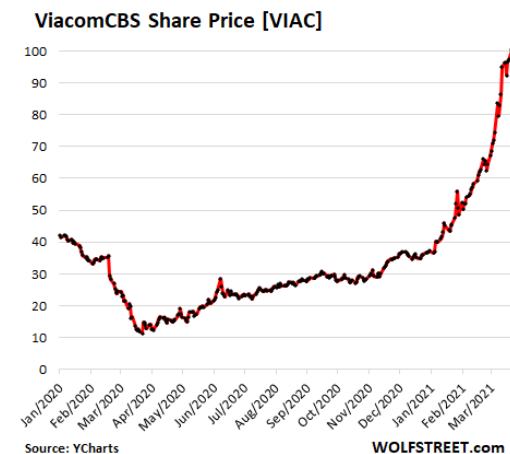
- March 2021: **Banks offering prime brokerage services to Archegos liquidated US\$ billions of various stocks after failed margin calls**
 - Stocks were tied to **total return swaps** held by Archegos
 - This sale was reported to be the **cause of a 27% plunge in share price of ViacomCBS and a similar fall in the price of Discovery**
- 29 March 2021: CS share price down 14%
- 6 April 2021: **CS reported losses of US\$ 4,7bn linked to Archegos**
- Later, CS **announced it would have to raise up to US\$ 2bn in fresh capital** to support its equity base
 - Reported **losses increased to US\$ 5.5bn** in late April **on a notional exposure of over US\$ 20bn ...**
 - ... or more than half of the bank's capital at the time ...
- Late April 2021: Bill Hwang and former Archegos CFO, Patrick Halligan, arrested on racketeering conspiracy, securities fraud, and wire fraud

Archegos Affair – A “Pump and Dump” Scheme on a Previously Unimagined Scale?

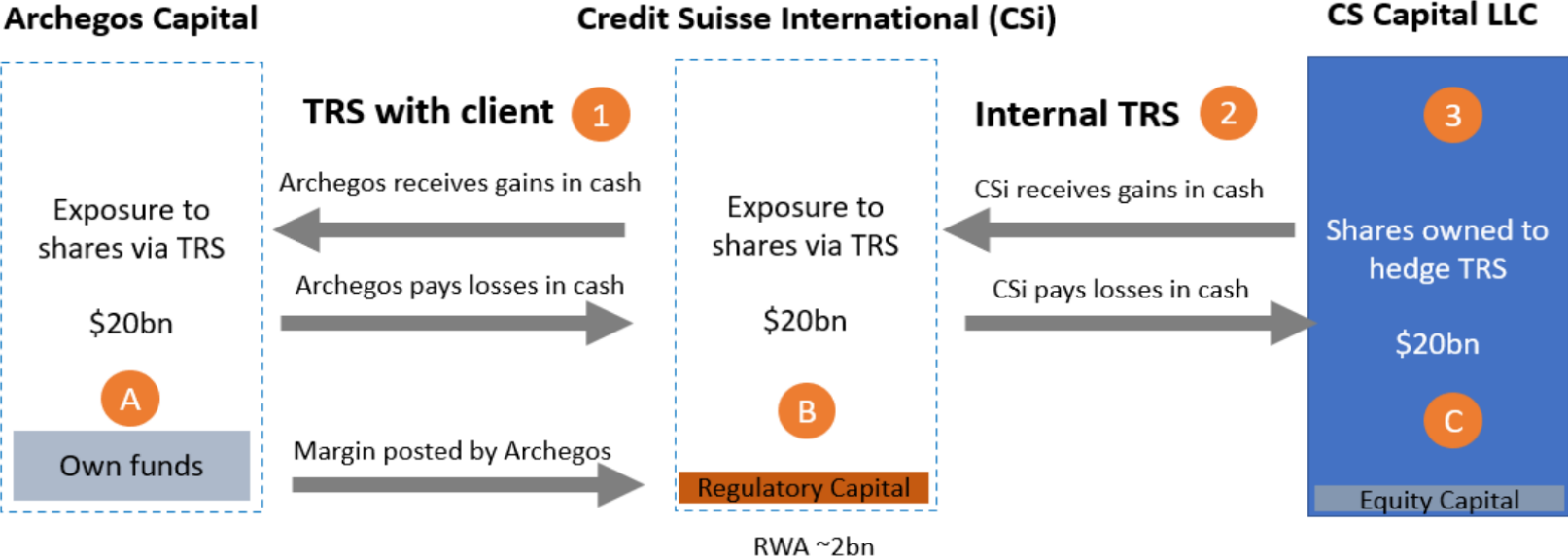
- According to an SEC complaint Archegos:
 - Bought huge, very **concentrated stock positions, mostly using money borrowed** from investment banks
 - Bought more of those same stocks indirectly, using **total return swaps** (again with borrowed money)
 - Thus avoiding public disclosure of these positions
 - Kept on buying those same stocks, directly and indirectly, to manipulative / support their prices
 - **Lied to get more loans from banks**, which would have been refused had they known how huge and concentrated the Archegos positions were

Ticker	Number of Shares ¹ (Market Value)			
	Jul. 1, 2020	Oct. 1, 2020	Jan. 1, 2021	Mar. 22, 2021
VIAC	49.3M (\$1.2B)	123.0M (\$3.4B)	185M (\$6.7B)	286M (\$28.6B)
BIDU-ADR	11.2M (\$1.4B)	22.3M (\$2.8B)	31.6M (\$6.6B)	55M (\$14.6B)
TME-ADR	59.0M (\$788M)	118.0M (\$1.8B)	210M (\$4B)	326M (\$10.0B)
GSX-ADR	19.3M (\$1.1B)	38.8M (\$3.6B)	70M (\$3.4B)	101M (\$8.5B)
VIPS-ADR	36.4M (\$759M)	79.0M (\$1.3B)	115M (\$3.2B)	169M (\$7.6B)
DISCA	3.0M (\$63M)	3.0M (\$65M)	60M (\$1.8B)	100M (\$7.5B)
IQ-ADR	67.2M (\$1.6B)	105.3M (\$2.4B)	155M (\$2.8B)	225M (\$6.3B)
DISCK	1.3M (\$25M)	1.3M (\$27M)	1.3M (\$34M)	91M (\$6.0B)
FTCH-ADR	6.4M (\$116M)	18.4M (\$500M)	37M (\$2.2B)	92M (\$5.7B)
SHOP-ADR	N/A	N/A	970 (\$1M)	1.7M (\$1.9B)

- In spring 2021 some of the stocks fell sharply in price, there were margin calls, and it all exploded ...



Excursion: Total Return Swaps



- 1 Total Return Swap (TRS) entered by Archegos with CSi
- 2 Total Return Swap (TRS) entered by CSi to transfer risk to CS Capital LLC (back-to-back transaction)
- 3 CS Capital LLC holds the underlying shares of \$20bn on its balance sheet, as a hedge for the TRS exposure
- A Own funds of Archegos, mainly cash margin provided to CSi as collateral
- B Regulatory Capital required by CSi, mainly driven by counterparty credit risk RWA of ~2bn
- C Equity Capital required by CS Capital LLC as U.S. registered broker dealer

October 2022 - The Big Restructuring

- CS announces a sweeping plan
 - Refocus on banking for the wealthy
 - US\$ 4bn capital raising
 - Headcount reduction of 9,000 jobs by end-2025
 - Separating out its investment bank to create CS First Boston
 - In the course of the US\$ 4bn fund raising, the Saudi National Bank took a 9,9% stake in CS



Revenues at investment bank and wealth management fall in bruising fourth quarter

- On Thursday, CS reported a **US\$ 1,5bn loss for the fourth quarter**, as
 1. **investment banking revenues slumped** and
 2. **clients pulled money** from the group's wealth management business
- The bruising quarter took the **bank's annual loss to SFr 7.3bn**
 - CS's **shares tumbled** as much as 16% to SFr 2.72, having fallen more than 69% over the past year and hit an all-time low of SFr 2.70 in December
 - **Customers withdrew SFr 111bn from the group in the final three months of the year**, with two-thirds of the outflows coming in October, when the bank was hit by rumours on social media about its financial health
 - The wealth management business accounted for SFr 92.7bn of the outflows in the quarter, the bank said, surpassing the SFr 61.9bn expected by analysts

14 March 2023 – Material Weaknesses in Financial Reporting Controls

“Management did not design and maintain an effective risk assessment process to identify and analyse the risk of material misstatements in its financial statements ...”

Annual Report 2022, CS

- CS had been forced to **push back the publication of the annual report** after receiving a last-minute call from the US SEC relating to cash flow statements going back three years, which it described as “technical”



15 March 2023 – Absolutely Not ...



No more money for Credit Suisse

That's what Saudi National Bank Chairman Ammar Abdul Wahed Al Khudairy told [@youseftv](#) when asked about more assistance for the troubled lender trib.al/GqsNDie



11:56 AM · Mar 15, 2023



1.2K Reply Share

Read 77 replies

15 March 2023 - “Whatever it takes” - SNB

- The Swiss National Bank SNB and the Swiss Financial Market Supervisory Authority FINMA assert that **the problems of certain banks in the USA do not pose a direct risk of contagion for the Swiss financial markets**
 - The strict capital and liquidity requirements applicable to Swiss financial institutions ensure their stability
 - CS meets the capital and liquidity requirements imposed on systemically important banks
- If necessary, the SNB will provide CS with liquidity

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FT Alphaville Credit Suisse Group AG + Add to myFT

Regulators say Credit Suisse is fine so please chill

“Whatever it takes” - SNB

© REUTERS

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FT Alphaville MARCH 15 2023 24

16 March 2023 – CS to borrow up to SFr 50bn from Swiss Central Bank

- CS plans to borrow up to SFr 50bn from the SNB and **buy back** around US\$ 3bn of its **debt**
- SNB willing to provide a liquidity backstop after **CS's shares fell as much as 30%**
 - The sell-off came **after** the chair of the **Saudi National Bank**, a major CS shareholder, **ruled out any further investment**
- CS said it had taken the decision to borrow the funds from the SNB under a loan facility and a short-term liquidity facility



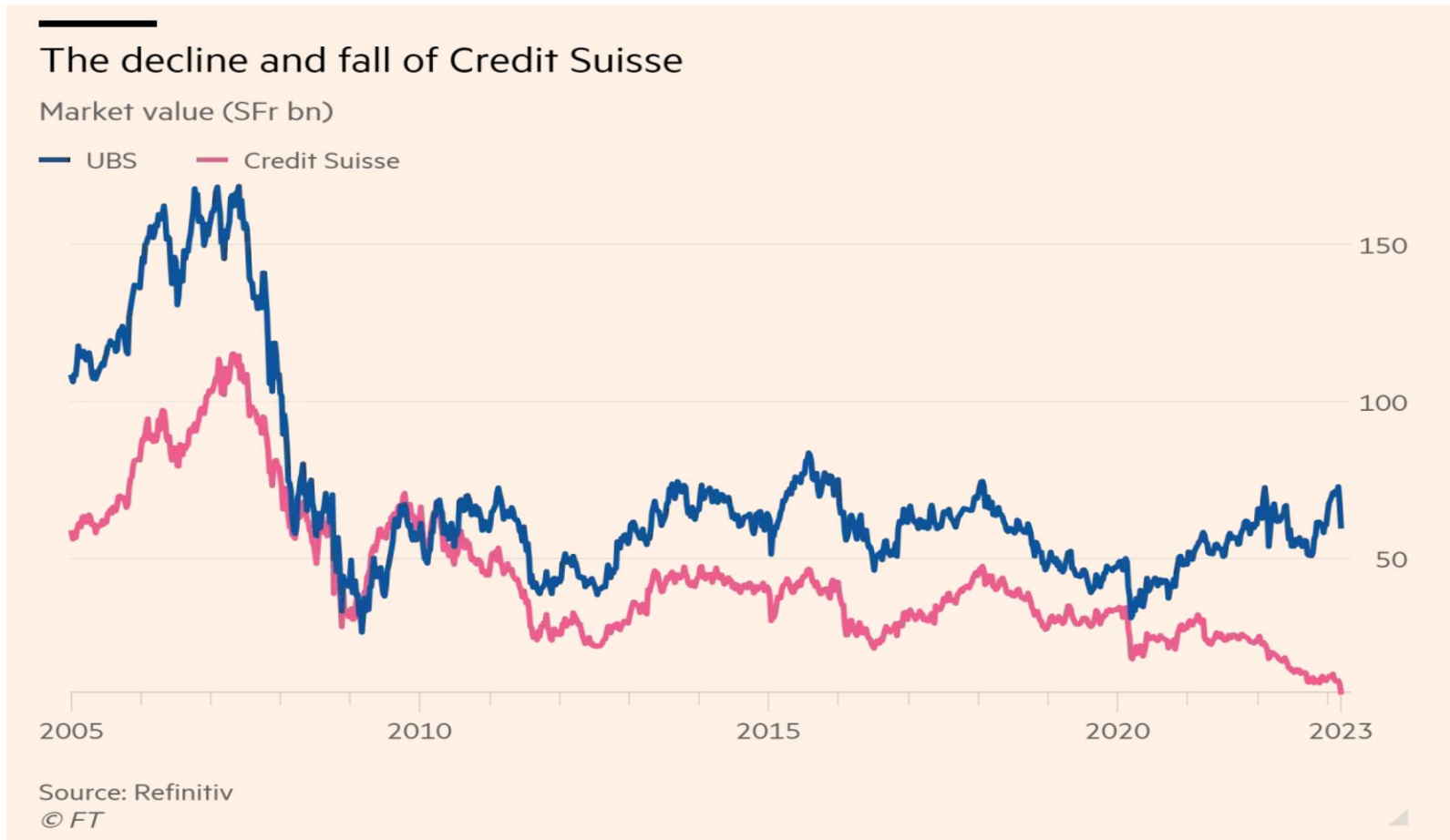
19 March 2023 - UBS agrees US\$ 3.25bn Rescue Deal for Rival Credit Suisse

“On Friday the liquidity outflows and market volatility showed it was no longer possible to restore market confidence, and a swift and stabilising solution was absolutely necessary,”

Alain Berset, Swiss President



UBS vs CS Share Price Dynamics



Deal Aspects

- **UBS will pay about SFr 0.76 a share in its own stock**, worth SFr 3bn
 - Up from a bid of SFr 0.25 (US\$ 1bn) earlier rejected by the CS board
 - Far below CS's closing price of SFr 1.86 on Friday
- **Creates one of the biggest banks in Europe**
 - UBS has US\$ 1.1tn of total assets on its balance sheet and CS has US\$ 575bn
- **SNB SFr 100bn liquidity line** backed by a federal default guarantee to UBS
- **Government loss guarantee of up to SFr 9bn**
 - **With UBS bearing the first SFr 5bn of losses** on certain asset portfolios
- Holders of US\$ 17bn of CS **additional tier one (AT1) bonds will have their entire investment wiped out**
- UBS has agreed to buy CS with Swiss authorities poised to **change the country's laws to bypass a shareholder vote** as they rush to a deal

Excursion: Selected Deal Issues – It's Not CS Shareholders Fully Wiped Out ...

- Holders of US\$ 17bn of CS **additional tier one (AT1) bonds will have their entire investment wiped out**
 - Order by Swiss financial regulator Finma: “The extraordinary government support will trigger a complete write-down of the nominal value of all AT1 bonds, and thus an increase in core capital.”
- Appeared to surprise markets
 - AT1 bonds had marked up significantly after UBS's takeover was confirmed, in expectation that the deal would not result in losses for bondholders ...
- AT1s were introduced as part of the post-global financial crisis regulatory reforms that pushed banks to increase their capital levels
- Form of contingent convertible security (“**coco**”), which **can be converted into equity if a bank runs into trouble**
 - If a bank's capital ratio falls below a predefined threshold, AT1 investors can lose their principal or have their investment converted to equity
 - As the riskiest form of bank debt in Europe, AT1s typically offer higher yields than safer bonds

Excursion: Selected Deal Issues – Shareholders Will Have No Vote

- UBS has agreed to buy CS with Swiss authorities poised to **change the country's laws to bypass a shareholder vote** as they rush to a deal
 - Emergency measures to fast-track the takeover and plans to introduce legislation that will bypass the normal six-week consultation period required for UBS shareholders

“I can’t believe our members and UBS shareholders will be happy about this. I have never seen such measures taken; it shows how bad the situation is.”

Vincent Kaufmann, CEO Ethos Foundation
Representing Swiss pension funds owning
3-5% of Credit Suisse and UBS

Excursion: Switzerland, It's One Big Bank ...

- **UBS alone will account for approx. 250% of Switzerland's GDP..**
 - ... a challenging “too-big-to-fail” risk for the country
 - **Switzerland's banking system's total assets are equivalent to 520% of the country's GDP ...**
 - ... a far higher proportion than any other major developed country
- Domestically there is a related risk for **retail banking** thanks to a competition waiver on the deal
 - JPM estimates the combined bank will have around **30% of the market**

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UBS Group AG + Add to myFT

Majority of Swiss want new UBS-Credit Suisse mega bank split up

Results of poll add momentum to calls for a review of the forced merger and for the clawing back of bonuses



About 47% of respondents in the poll strongly agreed with the statement: 'UBS is now too big. It should be split up because of the risks' © Stefan Wermuth/Bloomberg

... for (entirely) personal reasons, of course ...



The screenshot shows a news article from the Financial Times. The header includes the Financial Times logo and 'myFT'. The article is dated '37 MINUTES AGO 08:45'. The title is 'Saudi National Bank chair resigns following Credit Suisse comments'. The author is 'Simeon Kerr in Dubai'. The article text states that Ammar Alkhudairy, chair of Saudi National Bank, has resigned for personal reasons after the kingdom's largest lender was thrust into the limelight amid the tumult at Credit Suisse. It also mentions that Saeed Al Ghamdi will replace Alkhudairy as chair, and Talal Al Khereiji becomes acting chief executive. Earlier this month, Alkhudairy said in a TV interview that SNB, which bought a stake just under 10 per cent in Credit Suisse last year, would not provide any more financial assistance. He said purchasing more shares would have pushed SNB's stake above 10 per cent and caused a "regulatory issue". His comments sent Credit Suisse's share price into a tailspin, eventually leading to its rescue by Swiss rival UBS.

In Banking, Trust is Everything

Contact

www.christianschopper.com
christian.schopper@christianschopper.com

CorpFinCE

Corporate Finance Central Europe

www.corpfince.com
christian.schopper@corpfince.com

