CRAIN'S DETROIT BUSINESS

March 17, 2023

by Nick Manes

Smaller banks, startups focus on diversification in wake of bank collapses

Customers line up outside Silicon Valley Bank headquarters in Santa Clara, Calif., on March 13, after the collapse of the bank prompted federal regulators to make moves to contain the fallout in the U.S. banking system.

Needless to say, it's been a busy week for global financial executives.

Multiple banks have collapsed since last Friday, largely those with significant asset sensitivity and too many eggs in their proverbial basket. More banks, including San Francisco-based First Republic, have been on the edge of significant trouble and on Thursday got a significant injection of deposits — $30 billion — from some of the largest banks in the country.

While the impact has been felt locally and many are taking stock and assessing what comes next, some say it's business as usual. For starters, Michigan's community bankers say they're sticking to their guns following the tumult of the last week.

Related

Comerica among 6 banks Moody's is reviewing over uninsured depositsMichigan investors plot path forward after Silicon Valley Bank's demiseFeds move to stop potential banking crisis, Biden urges stronger rules

While fully cognizant of the impact of multiple bank collapses in a short period of time, local executives say they see few parallels between how they operate their lending institutions and what's known about the circumstances that brought down Silicon Valley Bank and at least two other banks, largely with concentrated ties to the tech industry.

Swiss banking giant Credit Suisse also appears to be teetering into the danger zone, albeit for reasons largely separate than what brought down SVB, as well as Signature Bank and Silvergate.

"It's amazing the different business models we all have, but we're all called banks," said Dave Lamb, president and CEO of Oxford Bank in northern Oakland County with about $792.6 million in total assets. "The No. 1 business we're all in is (managing) risk. We should never predict the future. And the answer to that is diversification."

Other executives at Michigan community banks — institutions generally with less than $1 billion in assets, placing them on the much smaller side of the banking world — offered a similar critique as Lamb.

At Chelsea State Bank, a community bank in western Washtenaw County with about $125 million in assets, “discipline” is the name of the game, according to President and CEO Joanne Rau, who said that calls from concerned customers have been few.

“For us, there aren’t big red flags in front of us,” Rau said of the recent events. “While customer needs may change, staying true to the fundamentals of banking are essential.”

At Oxford Bank in northern Oakland County, deposits have remained “consistent with previous weeks,” its CEO said.

Banks in Michigan’s small towns like Chelsea and Oxford play in a very different world than a bank like Silicon Valley Bank. While the 16th largest bank in the country with over $200 billion in assets, SVB was still very much just a regional bank.

Because SVB had less than $250 billion in assets, it fell short of many of the regulations put in place under the Dodd-Frank Act, which today largely polices just the largest banks in the country.

Attempts by Crain’s to interview executives with many of the larger regional banks operating around Michigan were unsuccessful. Spokespeople with banks including Comerica, PNC, Huntington, Fifth Third and others declined interview requests or said executives were unavailable.

Spokespeople with Huntington and Fifth Third — both headquartered in Ohio, but each among the largest banks operating in Michigan — provided separate statements saying their operations have been unaffected by the events of the last week and the banks see no indication of the troubles that have befallen Silicon Valley Bank and others.

Dallas-based Comerica, another large regional bank with a significant Michigan presence, has been listed by Moody’s Investor Services as one of a handful of banks the ratings agency is reviewing for potential trouble. The ratings agency has cited concerns over the lenders’ reliance on uninsured deposit funding and unrealized losses in their asset portfolios.

A Comerica spokesperson earlier this week, and again on Thursday, took issue with the bank’s presence on the list of banks being reviewed by Moody’s, writing “that any correlation between Comerica and the recently impacted banks in regard to deposits is an apples-to-oranges comparison.”

Taking a step back, while being careful to not “underestimate the interconnectedness” of the global financial system, Nick Juhle said he believes the instability being experienced this week is likely to be relatively confined.

“There’s plenty of uncertainty out there,” said Juhle, the chief investment officer of Greenleaf Trust, a Kalamazoo-based trust bank and wealth manager with offices around the state. “But a repeat of the global financial crisis? That still seems like a little bit of a stretch to us.”

Finding balance

So where does the trouble lie?

At least in the case of Silicon Valley Bank, the issue appeared to be an over-reliance on deposits from the tech sector and poor risk management that failed to see the diminishing value of assets acquired with those deposits.

An announcement by the bank last week that it needed a capital injection led to a bank run and the ultimate collapse last Friday, which ended with regulators taking over the bank and ultimately guaranteeing all deposits.

Such a business model is vastly different at a lender like Oxford Bank, its CEO said.

“The difference in community banks is we’re very granular,” Lamb said. “Our customers are granular. We can’t be concentrated in deposits.”

The goal, according to Lamb, is to “balance” between liabilities — loans — and assets.

“If the world changes on you, you don’t have one side or the other reprice on you,” he said, referring to how the value of both can change, largely from interest rate fluctuation.

Still, the tumult has led to some opportunity for banks, particularly larger ones, such as Bank of America. A Bloomberg report this week said the Charlotte, N.C.-based bank had mopped up more than $15 billion in new deposits in a matter of days, emerging as one of the big winners after the collapse of three smaller banks dented confidence in the safety of regional lenders.

The statement from Fifth Third Bank, sent to Crain’s on Thursday, also alluded to increased deposits and new customers opening accounts, but a spokesperson did not provide an amount.

Lamb told Crain’s that deposits at his bank have been “consistent with previous weeks,” and noted that’s what he has heard from colleagues in the smaller community banking space.

Like others, Rau with Chelsea State Bank expressed a general sense of optimism for conditions going forward, but acknowledged an economic downturn is likely in the coming months.

“Do I think a recession is in sight? All the investment banks have been talking about this for a year and a half,” Rau said. “I do believe we’ll likely be in a recession, but I don’t think will be a hard landing like 2008 or 2009. Maybe that makes me a little naive, but looking at where we stand in Southeast Michigan, I feel pretty good. But I’m cautious as well.”

‘A void’ in the startup space

Beyond the banking world, other industries are also closely monitoring the instability in financial markets. That’s particularly true in venture capital, an industry that had a close relationship with Silicon Valley Bank going back decades prior to its collapse and government takeover.

Much of Silicon Valley Bank’s book of business was tied to banking services tailored to the needs venture capital funds and their portfolio companies.

Farmington Hills-based Beringea — the state’s largest VC fund with about $750 million in assets under management, according to Crain’s data from 2021 — did have portfolio companies unable to access their money following the bank run at SVB, according to Michael Gross, Beringea’s managing director.

The first step that executives at Beringea are taking, Gross said, is “tactical” changes and changing up the fund’s “treasury strategy” to ensure holdings aren’t overly concentrated at any one bank.

But at a larger level, the death of SVB — which has yet to secure a buyer — is something that will likely create challenges for startups and investors going forward, he said. One of the key services the bank provided was debt lending to startups, essentially bridge capital a company could raise to tide over operations in between equity rounds.

“While it wasn’t venture lending that caused the (collapse of SVB), the outcome is venture lending will get tougher to secure, or go away all together,” Gross told Crain’s, noting that the overall landscape for venture capital investment has cooled amid the period of higher interest rates. “That will leave a void in the industry at a time when it’s critical for companies.”

Small business consultants told Crain’s that their clients are taking notice and watching the bank instability, but it’s “front page stuff” like interest rates, inflation and finding workers that continue to be the largest challenges, according to Brooks Kindel, a business growth consultant with the statewide Michigan Small Business Development Center, housed with the Seidman College of Business at Grand Valley State University.

The goal for many of his clients — which range from bars and restaurants to manufacturers and professional service companies — and are largely “doing quite well,” he said — is to focus on “hardening their business” to provide as a hedge against the types of events that have played out this past week.

“They’re trying to reduce risk, reduce debt, fire unprofitable customers,” Kindel said. “They’re trying to do all the things you need to do to protect your margins. That helps provide a sense of a little more calm or confidence.”

— Bloomberg contributed to this report