<u>The Outlook: March 10, 2023</u>

Live by hot money . . . die by hot money.

The Market Since 2022

That red circle, and the crocodile-teeth whipsaw inside it, is the picture of a market which has been trying on Nightmares for size since 2022 began, pretty much. The Nightmares have ranged from "Inflation Monster Arrives!" to "Federal Reserve on the Warpath, Main Street Doomed!" to this week's "Silicon Valley Bank Collapses! Global Bank Runs on the Way?" The Nightmares each have their kernel of truth, as all good Nightmares do: kernels just large enough to distort the truth of things beyond all recognition . . . as always.

We all know the first two Nightmares like old friends, since they've been trying to haunt us for the last 15 months. The latest, "Bank Collapses! Panic on the Way?" is worth a glance, only because it's the latest.

A very long time ago a young banker, fresh out of grad school, asked an old banker what an old saying meant: "Live by hot money . . . die by hot money." It meant, he explained, that banks were always tempted to bring in new deposits the easy way: in million-dollar chunks (or more) rather than thousand-dollar chunks, one household at a time, earned by the slow, painstaking process of meeting people, setting up checking and savings accounts, making a car loan and so on. The trouble was that the million-dollar chunks were quite often controlled by people or institutions which wanted the last tenth of a percent of interest on their money, and were very willing to yank the money (yup, that million dollars at a time) whenever they spotted a different bank offering a tenth of a percent more. "Hot money" indeed. So any bank which bid for the hot money had better be ready to lose it on a moment's notice, which meant investing the million-dollar hot chunks in assets paying so little they were hardly worth it.

The "dying by hot money" happened when the bank gave into temptation to buy a more profitable asset with the hot deposits—which always meant running the risk of loss if the asset had to be sold in a hurry. That brings us to the last old saying, from Wall Street: "Bulls make money. Bears make money. Pigs get slaughtered." Of course that's Wall Street's colorful way of saying "Don't get greedy." Silicon Valley Bank's reason-for-existence, pretty much, was to cater to the vast pools of "hot money" sloshing around Silicon Valley—where plutocrats with big egos get a kick out of writing galactic-sized checks to fund interesting-sounding startup companies in the Tech World. It would be good business, if more than one per hundred lasted long enough to turn a profit. They don't. But none of that bothered Silicon Valley Bank, which must have figured the magic of its name might cool off the hot money, so that the Bank might live rather than die.

This week it found out differently when the hot money ran, and it's gone, leaving the market its Nightmare of the Day to chew on, for a while. But what about "Global Bank Runs on the Way?"

Well, in the market anything is possible . . . briefly. "Bank Runs!" is a pretty good Nightmare, and the betting crowd is wondering, as we speak, whether it's good enough to bet on for a little while. The difference between that "little while" and "long enough to really hurt" lies with cold facts, as always. Main Street's banks are financially stronger than any banking system has ever been, in U.S. history and beyond. Washington DC has never stopped jumping up and down on them since 2008 – 2009's Great Financial Calamity. It's been a very good way for politicians and regulators to be seen to be doing something virtuous for the public. The effect has been, fundamentally, that the US banking system has stuck largely to those hard-won thousand-dollar chunks of new deposits. Once those dollars arrive and get tied down with checkbooks and mortgages . . . they're pretty darned "cold." It takes a lot to bother them enough to leave. "Silicon Valley Bank Collapses!" won't do it, because the facts are that Silicon Valley Bank got greedy, not JP Morgan Chase, Bank of America or any of that crowd.

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