

PALOS

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Weekly Commentary

Issue Special | MARCH 17, 2023

By Charles Marleau CIM[®] and William Mitchell CIM[®]

Special Issue: Safety in Canadian Banks

Along with virtually every investor around the globe, we are closely following the turmoil in the banking sector. Last week, San Francisco based **Silicon Valley Bank (SVB)** and New York based **Signature Bank (SBNY)** dominated headlines with reports that they had failed. The news ignited a swift “run on the banks” reminiscent of a scene from Frank Capra’s epic film “It’s a Wonderful Life”. With confidence shaken and uncertainty plentiful, panicked clients and investors made a rush for the exits.

We thought it would be a good idea to share our perspectives with you. To do this, we have highlighted some facts about the evolving story that we have cited below. This should offer some clarity and peace of mind.

- 1. Canadian banks are different.** There are over 4,000 banks in the United States. The current crisis is constrained to the smaller regional banks that operate in specific areas of finance. They are not as well diversified or as well capitalized as their larger peers (i.e., the Majors) that are designated as “too big to fail”. Furthermore, their problems are self-inflicted. Imprudent risk management, dislocation in bond maturities, and supervisory failure is what led to their downfall. The Canadian banking system is very different. Our banking industry is dominated by six federally chartered banks that are extremely well capitalized, highly regulated, diversified across all aspects of finance, and operate on a national (and international) basis. Our banks are recognized around the world as conservative, supervised, and safe.
- 2. This is a crisis of confidence.** Governments and industry participants have pledged support as fears grow. On the heels of the SVB “flight to safety”, the Federal Deposit Insurance Corporation (FDIC) announced that all deposits would be guaranteed. This was intended to calm nervous depositors. First Republic (FRC) is an example of another “regional” bank that has been impacted as depositors flee to larger banks. To stem the outflows and demonstrate confidence in the banking system, a group of America’s largest financial institutions has deposited \$30 billion into accounts at FRC. The group includes JP Morgan, Bank of America, Wells Fargo, and Citigroup contributing \$5 billion each.
- 3. Exposure to non-Canadian banks.** Here’s an update on Palos’ exposure to the banking sector. Apart from some individually managed portfolios, our proprietary funds are focused on Canadian banks.

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Exposure to U.S. banks, mostly held in individually managed mandates, is limited to only the best capitalized and operationally diversified institutions, namely, JP Morgan Chase and Bank of America. These are amongst best capitalized banks in the world. In fact, the “majors” are seeing an unintended benefit as depositors move money from small banks to large banks. In our view, this is a long term positive for the larger banks.

Should you wish to discuss your investments or if you have any questions, it would be our pleasure to discuss these with you personally. Palos portfolio managers are available to meet at your convenience, either in person, by telephone or through a virtual meeting using Microsoft Teams.

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