CNN AUDIO

Episode Transcript

CNN One Thing

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Breakdown of a Bank Collapse (and What It Means for You)

Speakers: Callie Christensen, David Rind, Kelly Oriard, Christine Romans, Alison Greenberg, President Joe Biden, Larry Summers

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Callie Christensen Kelly and I were actually at a toy industry media event in New York City on March 8th.

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David Rind This is Kelly Christensen. She's the co-founder of Slumberkins. It's a kids toy company. They make these cute stuffed animal characters and corresponding books that teach emotional learning skills. And it was on March 8th, a little over a week ago, when she and her co-founder, Kelly Oriard, started hearing that her company's bank might be in a little bit of trouble. You'll never guess which one.

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Callie Christensen And on Thursday, though, tried to access our accounts at Silicon Valley Bank, and the portals kept crashing.

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David Rind The next day, as they were about to board a cross-country flight back home to Portland, Oregon, Silicon Valley Bank confirmed their withdrawal request. But that's all they knew.

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Callie Christensen And we got on the plane thinking, okay, our our entire bank account is hanging in limbo in a wire transfer fund. We hope it materializes by 5 p.m. at the end of today.

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Kelly Oriard Yeah. And in that timeframe, we hear that the bank failed and it's it's gone under. So that was like, wait a minute, what? How do we what are we supposed to do that can kind of. Can your money just go poof?

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David Rind Callie and Kelly had found themselves in the middle of the largest U.S. bank failure since the financial crisis of 2008. They told me their thoughts immediately turned to basic questions like, Where are we going to get enough money to keep the lights on? How are we going to pay our 30 some odd employees?

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Kelly Oriard There was a moment where just out of fiduciary responsibility, one of our board members said, Well, we should have a wind down plan just in case. And I think that's what set Kaylie and I into crazy Mama bear mode of saying, No, we're not going to start a wind up.

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David Rind Wind down. Meaning like this is over.

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Kelly Oriard Yes.

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David Rind Now it's not over for Slumberkins or the other depositors who did business at Silicon Valley Bank. The Biden administration stepped in to ensure depositors would have access to all their money, even those above the $250,000 insurance limit. But the run on SVB has shaken the entire banking system to its core and rattled the confidence of some business owners like Callie and Kelly.

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David Rind Obviously with the startup culture, like, things can kind of flame out fast. Did you ever feel like that was a possibility with with a bank like this that kind of dealt in that world?

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Kelly Oriard I don't think that the thought really crossed my mind that a bank would flame out.

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David Rind My guest this week is CNN chief business correspondent Christine Romans. And we're going to unpack all this, how we got here, the government response and if the collapse will influence the Fed's fight against inflation. From CNN, this is One Thing I'm David Rind.

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David Rind Christine, I want to warn our listeners right off the top there, just like a lot of acronyms in this story. It's kind of like alphabet soup. But I'm glad you're here because you know what they stand for. So you can help us out. It's been over a week now since Silicon Valley Bank failed. For those who have not been following, like beat by beat. How did we get here?

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Christine Romans Let's have a swear jar and we'll put a dollar in for every acronym and every piece of jargon. Banking, jargon. What happened was this bank called Silicon Valley Bank, failed spectacularly in 24 hours. And it's a niche bank. It banks for venture capitalists startups. I mean, most people have never even heard of it.

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David Rind It's not like the average mom and pop.

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Christine Romans No, no. And suddenly it went down, twisted. And here's why. It has to do with its super safe investments for years with 0% money, right? Free money, low interest rates. The startup world was booming. The venture capital world was booming. And all that money was going into Silicon Valley Bank, all these deposits. The bank management took those deposits and put them in super safe treasuries, long dated treasuries. You could hold them for ten years and then you sell them very safe. Except suddenly there was a downturn in tech and those startups started burning through cash and withdrawing their money as they withdrew their money. The bank had to come up with money and sold some bonds at a loss that triggered concern about the viability of the bank and a run on the bank. It all happened so fast.

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David Rind People got afraid that their money wouldn't be there, so they went to go pull it out.

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Christine Romans And they pulled it out quickly.

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Alison Greenberg The email seemed cryptic. It was strange, it was urgent, and he said, Take your money out of SVB, go into your account, take your money out as soon as possible.

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Christine Romans And it's different than Washington Mutual, the largest bank failure in the U.S. in 2008 that took ten days. And in ten days, depositors pulled out $16.7 billion. Last week, depositors pulled out, tried to pull out $42 billion in one day because of, look, text messages, Twitter, social media and online banking. They were quickly using technology to get their money out. So it was the first tech run we've ever seen.

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David Rind There wasn't necessarily lines.

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Christine Romans Exactly.

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David Rind In front of the bank. They just go on their phones and do it.

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Christine Romans Exactly.

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David Rind
And people will be looking at bank to see, hey, is my money safe? We know from what happened at SVB, these things can move very quickly. Well, so what did the government do about it?

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Christine Romans
So after a couple of days of kind of wringing their hands, quite frankly, wondering if there was going to be what we call systemic risk, they decided to make the depositors whole. So, as you know, the Federal Deposit Insurance Corporation, the FDIC. A dollar in the jar, the FDIC insured deposits up to $250,000. This bank, SBB, I think 87% of its deposits were above that limit.

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David Rind
Big money.

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Christine Romans
Big money. You know, we're talking about flower delivery companies and we're talking about companies that work on Etsy, Roblox, for example, Roku, some of the names you might know. And so this was going to be a problem for their employees and for their payroll. So the government stepped in and said, we will insure all of those deposits, but.

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President Joe Biden
No losses will be borne by the taxpayers. And we repeat that no losses will be borne by the taxpayers.

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Christine Romans
We are not going to bail out the bank. We will bail out the depositors.

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President Joe Biden
Investors in the banks will not be protected. They knowingly took a risk. And when the risk didn't pay off, investors lose their money. That's how capitalism works.

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Christine Romans
And so the depositors will be made whole. Bank management fired and the government took over. A second thing happened to the Federal Reserve, created a new facility lending facility, as it's called. So if you're one of these banks with these long term safe but long term treasuries and you need to sell them at a loss, you can now go to the Fed and say, hey, I need a loan on what these bonds I think they should be worth, not what the market thinks they're worth. So the Fed essentially is giving favorable loans for a year so banks don't have to sell those assets.

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David Rind
Hmm. So did all that stuff work?

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Christine Romans
I think it worked. I think it stopped the bleeding. And I'll tell you, there are fundamentals in banking which are solid. They're a strain. I mean, Moody's Investors Service has put the whole the whole sector on watch for weakness because of the pressure from these higher interest rates. But it's the fear that was the big problem and how quickly it spread. We hadn't seen it spread like that. So the fundamentals are different than the fear and the fear. The fear is the harder thing to stop.

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David Rind
Hmm. You mentioned the B word earlier. Bailout. Mm hmm. Was this a bailout? Because I know President Biden and the administration have gone to great pains to not say that word and say, like, this is different. So what? What's the distinction?

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Christine Romans
So those depositors who are going to be made whole venture. Capitalist startups. That money comes from an FDIC insurance fund that is paid for by bank fees. So the banking industry now, critics will argue, well, those banks are just going to turn around and raise fees for consumers so consumers would pay for it anyway. That's a big fight that they have. The full faith and credit of the U.S. government is behind that Fed facility. I told you so. That's why critics call that a bailout. But the White House and the Fed won't call it that. They'll say it was just simply a rescue, an important intervention to make sure that the economy isn't hurt and that helps everyone.

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David Rind
But does this just kind of let them off easy in the end, like incentivize this kind of behavior down the line? If the bank thinks that, oh, the government will just come in and make everybody happy at the end.

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Christine Romans

Yeah. And that's called moral hazard. And we learned about that after 2008. Remember 2008, some of these banks had ridiculously terrible investments on their books and they knew it. No one went to jail. No one really even lost their job. People got to keep their bonuses. Everyone got very rich selling this garbage and it took down the U.S. economy. No one wants that to happen again, which is why I bail out the word bailout is such a dirty word. The White House, the FDIC and the Fed Treasury officials say no because they punished the management. But on the flip side, what would have happened in the absence of stabilizing this, I guess we just don't know. And you could have just just as vocal hue and cry about why didn't the government do something to prevent this. You know, and then they do something that's well, this is just going to incentivize other people to take bad risks. So it's a little bit of a damned if you do, damned if you don't.

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David Rind

I want to take a step back here because the average person, like we were saying, probably does not do business at a bank like Silicon Valley Bank doesn't deal with those huge dollar amounts that we're talking about here. So are there wider concerns for the average customer at their average Bank of America, PNC, that kind of thing?

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Christine Romans

I'm going to say no, and I don't even think I'm going out on a limb to say that if you're a typical person with a typical bank account, you are covered by the Federal Deposit Insurance Corporation. The FDIC will insure your money up to $250,000. The drama comes for policymakers at the Federal Reserve who have to decide what to do about interest rates should they keep jacking them up. And for stock market investors, if you are an investor in one of these banks, you are getting hammered right now and you might have bank stocks in your 41k. So that could be a typical person's exposure, too.

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David Rind

And you mentioned inflation and that was kind of like at the root of like some of the bank's decisions was the interest rate. So what are we going to see now with interest rates going forward?

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Christine Romans

It's so fascinating because we have high inflation in this country. The prescription to cure high inflation is higher interest rates, but those higher interest rates are the things that are rattling the banks. So it's this circle. And what the Fed has to do is figure out how to kill inflation without disrupting the banks or breaking apart of the banking system.

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Larry Summers

I don't think this is a time for panic or alarm.

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Christine Romans

We talked to Larry Summers this week, the former treasury secretary.

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Christine Romans

Talk to us, Secretary Summers, about the inflation fight and how that should still be in the forefront of what the Fed is trying to do, in your view.

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Larry Summers

Look, Americans money is safe.

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Christine Romans

And I asked him how, you know, does the Fed need to slow down on interest rate hikes, you know, to keep the banking system safe? When a week ago, inflation was the biggest problem.

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Larry Summers

But we are still also seeing very substantial rates of inflation. And if those substantial rates of inflation continue, they will erode people's purchasing power and their ability to spend.

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Christine Romans

And he said inflation is a threat to American families. Worries about your money and your bank is just a fear. One of those things is real. The other thing is psychological. So inflation is still the big job here, and the Fed needs to keep raising interest rates.

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David Rind

And what is the state of inflation right now?

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Christine Romans So it's cooling, but still too high. Consumer inflation. The consumer Price index. CPI, dollar. And that's where our CPI is running about 6%. That is three times what the Fed would like to see. Peppy producer price index. That's factory level inflation. This week we learned it's 4.6%. That's cooling faster. That's good. That's good news and good for the Fed because it shows that maybe all those rate hikes are beginning to work. But the Fed next meets March 22nd and has a lot to consider here.

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David Rind But what are they going to do?

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Christine Romans So I would have said a week and a half ago we should be prepared for a 50 basis point rate hike. Today, the consensus seems to be more like a smaller rate hike to continue to tap the brakes on the economy, to try to cool off inflation at the same time, not to go so much that you risk exposing some weakness in the banking sector that we don't see. Fundamentally, the banking system is much better than it was in 2008 and the economy is good. I mean, what was lost in all this is the underlying economy is still so strong. That's why the Fed has been raising interest rates like this, trying to cool it off.

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David Rind Cause it's gotta pump the brakes. It's like, okay, you're doing too good, right?

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Christine Romans Exactly. The job market still strong. Inflation's still too high. It's a very delicate process. And the Fed really only has one very blunt tool, and that is, you know, raising interest rates. I've heard it likened to they've got a hatchet when you really need a scalpel, but all they have is a hatchet. But they're very concerned about inflation. Entrenched inflation is very hard to fix. And so that is really the enemy of growth. It's the enemy of of really raising standards of living in this country. So they're really trying to.

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David Rind You're saying it's not just like I'm paying more for eggs at the grocery store a few weeks, like it has reverberations down the line.

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Christine Romans It absolutely does. It can cool growth for years. It can be this thing, this lead blanket that hangs over an economy. And so they really want to get that back closer to their 2% target.

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David Rind Hmm. Christine, thank you.

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Christine Romans You're welcome.

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David Rind And one thing is a production of CNN Audio. This episode was produced by Paola Ortiz and me, David Rind. Matt Dempsey is our production manager. Faiz Jamil is our senior producer. Greg Peppers is our supervising producer. And Steve Lickteig is the executive producer of CNN Audio. Special thanks to Richard Davis, Kevin France and Jessie Jezewski. Thank you for listening. We'll be back next Sunday. Talk to you then.