Sunwest Bank

BUILT FOR ENTREPRENEURS BY ENTREPRENEURS

Market Data

Interest Rates

	Current	Month Ago	Year Ago
Bank Rates (As Of 5/31)			
WSJ Prime	8.25%	8.00%	4.00%
1 Month Term SOFR	5.16%	5.02%	1.05%
Fed Funds Rate	5.08%	4.83%	0.83%
30 Year Mortgage Fixed	6.57%	6.43%	5.10%
Treasury Rates (As Of 5/31)			
10 Year	3.63%	3.44%	2.86%
7 Year	3.69%	3.48%	2.87%
5 Year	3.74%	3.52%	2.82%
3 Year	4.03%	3.76%	2.72%
1 Year	5.17%	4.79%	2.06%
1 Month	5.32%	4.39%	0.76%
1-Month SOFR Term SOFR Swap Rates (As Of 5/31)			
10 Year	3.32%	3.28%	2.62%
7 Year	3.37%	3.31%	2.57%
5 Year	3.48%	3.40%	2.55%
3 Year	3.81%	3.70%	2.58%

Inflation Data

	Current	Month Ago	Year Ago
CPI Headline YoY	5.0%	5.0%	8.2%
CPI Core YoY	5.5%	5.6%	6.1%
PPI Headline	2.3%	2.7%	11.2%
PPI Core	3.4%	3.7%	6.8%

Economic Data

	Current	Month Ago	Year Ago
PMI Manufacturing	48.4	50.2	57.5
PMI Services	55.1	53.6	53.5
Case/Shiller U.S. Home Price Index	297.1	293.4	295.1
Housing Permits	1,416k	-1.5%	-21.1%
Housing Starts	1,401k	+2.2%	-22.3%
Retail Sales	$598b	+0.4%	+0.5%
Unemployment Rate	3.4%	3.5%	3.6%
Non-Farm Payrolls	+253k	+165k	+254k

Equity Markets (As Of 5/31)

	Current	Month Ago	Year Ago
DJIA	$32,908	-3.36%	0.29%
S&P 500	$4,180	0.29%	1.92%

LETTER FROM THE CEO

Aftermath of the Major Bank Failures: The Credit Crunch is Coming

The collapse of several large banks in 2023 caught the regulators and the markets by surprise. While cracks were foreseeable, exactly what would break first was difficult to predict. Years of low interest rates, massive government spending, and money printing by the Federal Reserve culminated in enormous amounts of public and private sector debts being financed at historically low interest rates. These dynamics mixed with a rapid spike in inflation created a financial powder keg.

The equally troubling dynamic is that management teams and boards of some of the largest banks in the U.S. had the view that the low interest rates of 2020 and 2021 could remain suppressed for a long period of time.

These banks, and likely many pension funds and insurance companies, purchased long duration securities and originated long term loans with terms of 10 to 30 years at historically low interest rates. The interest rate risk and mismatch embedded in U.S. financial institutions from these decisions went unnoticed until the failure of Silicon Valley Bank. Silicon Valley Bank wiped out all its capital because of the mark-to-market losses generated from the interest rate risk embedded in its securities portfolio. Similarly, First Republic Bank embedded their interest rate risk in their lending portfolio, which led to their failure. As a result, the failures of First Republic Bank, Silicon Valley Bank and Signature Bank represented the second, third, and fourth largest bank failures in U.S. history.

Few institutions took the degree of risk that Silicon Valley and First Republic did, which resulted in their failure, but the majority of the banking industry purchased and originated large portfolios of low yielding securities and loans over the past few years. As a result, with interest rates having risen by 5.25%, the banking industry and many other segments of the financial services industry have enormous mark-to-market losses embedded on their balance sheets, severely reducing their tangible capital levels.

The problem this presents to the economy is that the banking industry will be forced to reduce lending and providing credit to businesses, consumers, and real estate. As I mentioned last month, the banking industry is the lifeblood of the economy because they are like gas stations in that they provide the fuel, money, to the economy. The effects of credit tightening will reverberate through the rest of the economy as banks continue to try to shrink their balance sheets in order to improve their regulatory capital ratios. This is evidenced by the Federal Reserve's Senior Loan Officer Opinion Survey which shows tightening credit standards across the industry. Additionally, the funding costs of banks, their deposits and borrowings, have risen dramatically. The consequence of these two dynamics will make credit both much more expensive and difficult to obtain.

Unfortunately, as the economy weakens further during the remainder of this year and into 2024, the banking industry will also have to absorb credit losses on the loans they originated and the securities they bought. This will only worsen the credit contraction that is well underway.

My advice to you is to hunker down and make sure your balance sheet is in a strong position and, if you have financing needs, to get those arranged sooner than later. Lastly, partner with a strong bank like Sunwest that will be there for you in good times and bad times. At Sunwest, we keep a fortress balance sheet in order to be there for our customers in even the toughest of economic times.

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