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Government intervention in the banking system may come with a political price. In the wake of regulatory actions to guarantee all deposits at two failed banks and to create a new bank borrowing facility, investors and banks should expect increased supervision followed by regulatory changes. These changes will be nominally intended for larger regional banks, but the impact of any new regulatory requirements is likely to cascade down to smaller institutions.

On Sunday evening, regulators responded to the banking crisis with the creation of a new "Bank Term Funding Program" (BTFP), which will offer loans of up to one year to depository institutions. The regulators also announced the resolutions of Silicon Valley Bank and Signature Bank and that all depositors at both banks would be made whole. These actions will lead to a series of policy debates in Washington that should impact the banking sector longer term.

The action to protect all deposits at the two failed banks raises the question of whether Congress should lift the cap on deposit insurance (currently $250,000). The Federal Deposit Insurance Corporation cannot increase the limit unilaterally, so increasing deposit insurance coverage is a question for Congress. Deposit insurance limits were eased (or eliminated altogether) during the Great Financial Crisis, but the legal authority on which the FDIC acted in 2008 expired at the end of 2012. Sunday's announcement relied of a systemic risk finding but such a designation seems limited to specific institutions rather than enabling a system wide response. This could push Congress to consider raising to eliminating the deposit insurance cap. Whether Congress approves an increase is an open question. Some lawmakers will question a government guarantee of wealthy depositors when the average account size is well below the current deposit insurance cap. Other lawmakers will oppose the expansion of government guarantee of deposits on philosophical grounds. The political situation is fluid and political winds may shift as market conditions change, but currently, **the odds seem low that Congress will approve deposit insurance coverage for all bank and credit union deposits. A smaller increase (perhaps up to $500,000) or indexing deposit insurance to inflation seems to have a better chance of passing Congress.**

In the aftermath of the recent failures, **regulators may feel political pressure to increase both supervision and regulation of the banking industry.** The bank failures could be seen as a supervisory failure whereby regulators failed to adequately oversee the growth at the failed banks as well as the banks' liability management. Bank examiners will probably feel pressure to not let the same mistakes happen on their watch so it is likely the examiners will become more aggressive in overseeing other banks – regardless of size.

Regulators will also feel a wind at their back as they consider changes modifications in tailoring thresholds for larger banks, changes in bank capital and liquidity requirements, and changes to bank merger rules. Federal Reserve Board Vice Chairman for Supervision Michael Barr has already announced a comprehensive review of bank capital requirements. This review could be extended to include a review of liquidity requirements. Although changes in various rules will be nominally targeted at larger banks, community banks could see ripple effects in how they are regulated. **Bottom-line: the regulators' efforts to stabilize the banking system will likely cost the industry with increased regulation.**

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