Wealth management insights from Stifel's CIO Office

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WASHINGTON POLICY STRATEGY

Potomac Perspective

Currently, there does not seem to be adequate political will in Congress to temporarily increase deposit insurance. Even if the political mood shifts, Congress is unlikely to act quickly and probably would not act until mid-April. If Congress does increase deposit insurance, the increase will likely come with strings attached.

House Republicans are currently meeting on their agenda, so the markets could get clues from those meetings as to where the House GOP stands. Also, Treasury Secretary Janet Yellen and key lawmakers will speak this week at the American Bankers Association's Washington Summit which could be a platform for them to layout their plans.

Recently, there have been calls to temporarily provide unlimited deposit insurance. While it seems like a long shot that Congress would approve this, we take a look of the possible timing if Congress does indeed act, key lawmakers, events to watch, and what strings could be attached to any increase in deposit insurance.

It seems unlikely that Congress will act until mid-April (at the earliest) if it decides to temporarily increase deposit insurance. The House Financial Services Committee will hold a hearing on March 29 regarding the failures of Silicon Valley Bank and Signature Bank. Federal Reserve Vice Chairman for Supervision Michael Barr and Federal Deposit Insurance Corporation Martin Gruenberg will testify. It is unlikely that the House would consider deposit insurance legislation prior to this hearing – absent a significant deterioration in the current situation. Following that hearing, the House and Senate will both be out of session for the first two weeks of April for the Passover and Easter holidays, which would seem to push any consideration of deposit insurance legislation until the second half of April.

House Republicans are currently holding a retreat to plan their agenda for the coming months, and the banking crisis will certainly be discussed among the GOP members. We could get some signals of how House Republicans intend to proceed following the retreat.

Also, this week the American Bankers Association (ABA) will hold its annual Washington Summit this week. The agenda includes several key speakers. Secretary Janet Yellen will speak to the group on Tuesday. On Wednesday, the ABA will host several key lawmakers. Senate Banking Committee Chairman Sherrod Brown (D-Ohio), the committee's ranking Republican, Senator Tim Scott (R-South Carolina), House Financial Services Committee Chairman Patrick McHenry (R-North Carolina), and that committee's ranking Democrat, Representative Maxine Waters (D-California) will be among those speaking on Wednesday. **While it is unlikely that either chairman will propose unlimited deposit insurance (either on a permanent or temporary basis), their remarks could provide some hints on their plans and timing for any prospective legislation.**

One of the key House Republicans to watch is Representative McHenry. In addition to being the chairman of the House Financial Services Committee, he is an ally of House Speaker Kevin McCarthy (R-California). Also, early in his career, McHenry was seen as bit of a bomb thrower and voted against the initial TARP bill. However, McHenry has evolved into a serious legislator and will be a key player if there are to be any changes in deposit insurance coverage.

Looking back to the Great Financial Crisis (GFC) should remind investors and industry participants that Congress does not move at light speed even under the most stressful conditions. In 2008, the government-sponsored enterprises were taken over on September 6, 2008. Lehman Brothers failed on September 15, 2008, and AIG was bailed out in the following days. On September 18, 2008, Treasury Secretary Henry Paulson and Federal Reserve Chairman Ben Bernanke met with congressional leaders, explained the ramifications of the crisis, and urged Congress to intervene. On October 1, even with warnings of a possible collapse of the entire financial system, the House of Representatives initially rejected the Emergency Economic Stabilization Act of 2008 (aka the TARP bill). The bill did not pass until October 3 when the House reversed itself. Even under the warnings of economic calamity, Congress did not act immediately. Contrast that with the current situation in which Treasury Secretary Janet Yellen has described the banking system as strong. That description will not jolt Congress into action.

If Congress eventually approves a temporary increase in deposit insurance coverage, investors should be prepared for the possibility that Congress could make additional changes in banking regulation. Such changes could include:

- Repealing S. 2155, the legislation that raised the mandatory threshold for banks to be considered "systemically important" from $50 billion to $250 billion.
- Imposing additional restrictions on executive compensation for banks and possible additional tools for regulators to claw back compensation.
- Implementing some type of limit of return on equity for bank investors – the theory being that if a large portion of banks' liabilities are guaranteed, why should shareholders have potentially unlimited upside.

Although S. 2155 (aka the Crapo bill) passed the Senate with bipartisan support, several of the bill's original Democratic supporters are no longer in the Senate, and the rise of populist Republicans increases the odds of bipartisan efforts to impose new restrictions on the banking industry. **Regardless of whether one thinks a temporary increase in deposit insurance is necessary, investors and bankers should also consider what costs might be attached to any increase in the government's backstop.**

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