EFFICIENT GROUP

ECONOMIC COMMENTARY

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YOUR MONTHLY ECONOMIC UPDATE

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Another Lehman Brothers? Luckily not!

Welcome to the world of banking crises, where there is a consistent flow of money and the stability of a shaky Jenga tower! Here, banks can go from being the pillars of the economy to crumbling ruins faster than you can say "subprime mortgage". So, grab your wallets and hold on tight as we unpack the events that unfolded in March.

Banking crises have a long history, with notable events including the Great Depression in the 1930s, Latin America in the 1980s, Japan and South-East Asia in the 1990s, and, of course, the Global Financial Crisis (GFC) in 2008. These financial fiascos have been like a bad penny over the years that will just not go away. They have been caused by a range of factors, including inflation, unhealthy monetary policy, poor banking practices, and a lack of regulation, to name but a few. They have led to significant economic downturns, widespread unemployment, and poverty, but have also led to reforms and changes in the banking industry to prevent future crises. Despite previous efforts to increase oversight, the current banking fiasco, once again, highlights the need for ongoing vigilance in the financial sector.

The most recent events started with the startup-focussed lender, Silicon Valley Bank (SVB) Financial Group, previously the sixteenth largest bank in the United States (US), which became the largest bank to fail since the GFC in 2008. The reason for the recent collapse was owing to the US Federal Reserve's (Fed's) aggressive interest rate hikes over the last year, which crippled financial conditions in the startup environment in which SVB was a notable player. Unfortunately, other banks, such as Signature and Silvergate, followed suit as a potential bank run threatened the stability of the overall banking system. Financial markets initially contracted by 4% but, by the end of the month, when the dust had settled, markets made up more than the initial loss.

Investors may be excused for mistaking the SVB banking fiasco for the Lehman Brothers and the GFC. But even though there are similarities, there are also substantial differences. For one, the GFC was triggered by a combination of a housing bubble, subprime mortgages, a lack of regulation, and oversight problems. In contrast, the current fiasco has been caused primarily by the COVID-19 pandemic, the associated economic downturn, and the structural shift in monetary policy. Furthermore, there is the severity of the impact to consider. The GFC was a global event that led to a significant downturn in the global economy. The current fiasco, while serious, has been largely limited to the US. It has also been well contained by the US Fed, US Treasury, and the Federal Deposit Insurance Corporation, who have offered to provide support where needed. Hence, the recovery and optimism in stock markets.

Locally, despite the impact of load shedding, downgrades, and our recent greylisting, South African banks have been able to weather the ongoing global sell-off extremely well as they were already well capitalised with high levels of liquidity. Additionally, South African banks have some of the best reputations among global banks. In fact, First National Bank was recently awarded the strongest banking brand in the world, closely followed by Capitec Bank. Overall, there are risks and challenges, but the South African banking system is strong and well regulated.

It is because of reasons like these that we continue to favour South African and emerging market equities, especially at a time when developed markets appear shaky. Emerging markets are only now starting their growth engines.

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