Opinion **Silicon Valley Bank**

With the collapse of Silicon Valley Bank, tech may lose a vital organ

Institution played an important role in the sector's smooth functioning

RICHARD WATERS

There has been no shortage of people seeking to turn the financial implosion at SVB Financial into a Silicon Valley morality tale © Bloomberg

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The flood of cash into the tech start-up scene in recent years has led to persistent warnings of disaster. Most often, these have turned on the kind of meltdown that hit Silicon Valley at the turn of the century, when a stampede to make money on the early internet led to massive over-investment.

It's safe to say, though, that none of the disaster scenarios envisaged the kind of financial implosion that struck this week at SVB Financial, the parent company of Silicon Valley Bank.

As an institution that is estimated to work with half of local tech start-ups, its collapse presents an obvious threat. It led the head of Y Combinator, San Francisco's pre-eminent accelerator for early stage tech companies, to warn on Friday that Silicon Valley's start-ups could be facing an "extinction-level event".

In many ways, this looks like a familiar tale in the banking world: In pursuit of higher returns, SVB failed to notice what, in hindsight, seems an obvious flaw in its risk management. Its assets soared nearly three-fold in the space of three years as capital poured into start-ups and was deposited, in turn, at the bank. SVB put much of the money into longer-maturity bonds to generate a higher return. When interest rates rose, the market value of those investments slumped, leaving the bank with losses that, on paper, stood at $15bn at the end of last year.

Rather than sell the bonds and take a hit, SVB hoped to nurse its low-yielding bond portfolio through to maturity, suffering lower net interest margins along the way. The plan might have worked. But it emerged this week that the bank's start-up customers, facing more difficult times, had been drawing down their cash, forcing it to sell investments and take a loss. The resulting need for more capital set alarm bells ringing and led to a flight by depositors: By Friday morning, regulators had to step in and close SVB down.

Heading into the weekend, it was impossible to tell exactly how deeply this financial shock would hit tech start-ups with deposits that have now been frozen. SVB's surplus capital at the end of last year was roughly enough to absorb its notional losses at that stage. Even after a further $1.8bn hit it reported this week, the losses still look modest in the context of a total deposit base that stood, in December, at $173bn (though $42bn flew out the door on Thursday alone.)

Yet the losses could well escalate as regulators carry out a forced sale of the bank's assets. Even more damaging, for many start-ups, is the risk that their much-needed cash will be locked up indefinitely, leaving them unable to meet immediate commitments like staff salaries and forcing some to close their doors.

There has been no shortage of people seeking to turn this into a Silicon Valley morality tale. To some, it is another example of the tech world's hubris, and proof that the good times blinded the tech industry to some very real risks. Why, for instance, did a public company like streaming video outfit Roku leave $487mn on deposit at what until recently barely counted as a medium-sized bank in US terms?

To others, meanwhile, the fallout from the SVB collapse is a reminder of how Silicon Valley, which usually fights hard to escape the heavy hand of government regulation, is quick to ask Washington for support when a crisis hits. Tan, the tech accelerator boss who warned of extinction, urged tech entrepreneurs to write to their local Congressional representatives calling for immediate government help.

By late Friday, the finger-pointing also had begun. The run on the bank that laid SVB low has been held up as an example of the herd-like behaviour often displayed by tech investors. A number of venture capital firms urged companies they had invested in to take their cash out of SVB after the bank said it was seeking to raise more capital. A partner at one prominent venture firm told me such withdrawals had caused a crisis that was entirely avoidable. Meanwhile, more than a dozen VC firms had banded together to promise they would stand behind SVB in future, should another institution step in to bail it out — though a number of well-known Silicon Valley firms were not part of the group.

The scramble among VCs underlined a dawning sense that, if SVB is wound up, something irreplaceable may be lost. One investor described the bank as "like a left ventricle" for Silicon Valley's financial scene — not as visible as the VCs which supply the risk capital that has floated the modern tech industry, but vital to the sector's smooth functioning. It was founded 40 years ago to fill the void left by big banks that often baulked at lending to start-ups. The VC firms that banded together on Friday night hope that it's not too late revive the bank. But if it is, Silicon Valley will have lost an institution that has played an important role in its rise.

richard.waters@ft.com