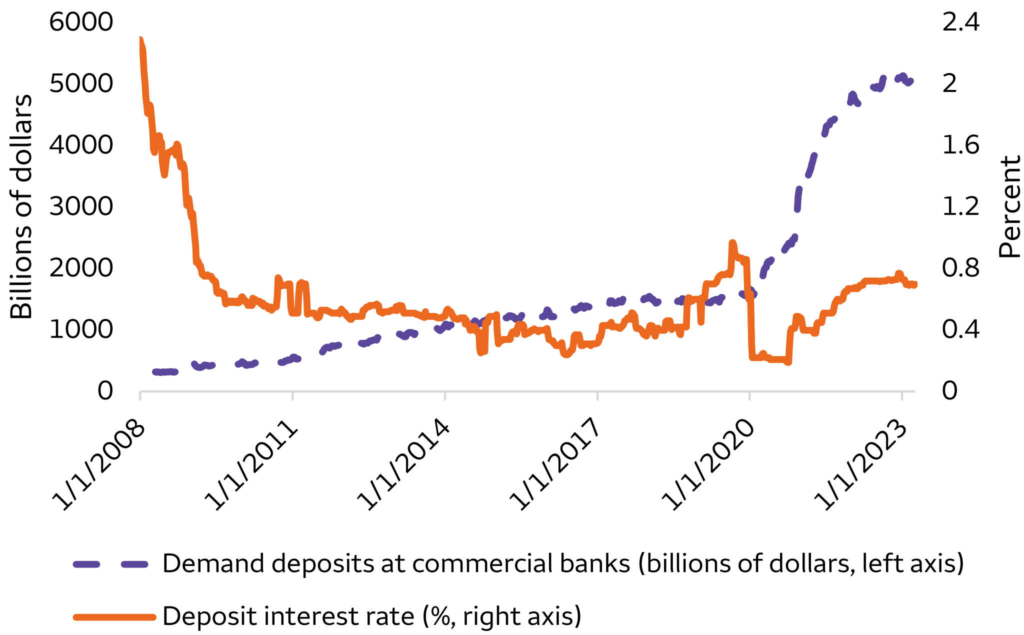
Chart of the Week

Weekly market analysis on key market indexes — May 9, 2023

Keep banking woes in perspective



Sources: Federal Reserve Board, Bloomberg, and Wells Fargo Investment Institute; weekly and daily data, January 1, 2008 – April 3, 2023. Deposits are shown as a four-week moving average. The deposit interest rate is the weekly average of daily U.S. deposit rates, averaged across the U.S. by Bankrate.

Surge in interest rates triggered higher costs for banks

As the chart shows, a dramatic decline in interest rates in 2020 encouraged a flood of bank deposits. Households banked government checks, and pervasive low interest rates made checking accounts attractive.

While rates stayed low during the pandemic, many banks used the extra cash to originate new mortgages or offer long-term bonds. But as long- and short-term interest rates have risen, assets such as mortgages and bonds have fallen in value, while bank costs, such as interest payments on deposits, have risen. These conditions created vulnerability for three of the four banks that failed in recent days.

What it may mean for investors

Although we may not have seen the last of failures among small and regional banks, bank stress is part of the current higher interest rate environment. In our view, the more pressing problem for investors is that higher interest rates and tightening credit are putting the economy on track for a recession. Meanwhile, we believe financial markets are underestimating the downside risk for equities. Because of this, on April 21, we reduced our exposure to equities and reinforced our defensive positioning in portfolios.

Paul Christopher, *Head of Investment Strategy*

This chart was excerpted from the *Institute Alert* report dated May 1, 2023.

Risk Considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Equities** are subject to market risk which means their value may fluctuate in response to general economic and market conditions and the perception of individual issuers. Investments in equity securities are generally more volatile than other types of securities.

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