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FDIC Issues Bank Failure Post Mortem Report

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Last week, the Federal Deposit Insurance Corporation ("FDIC") issued a report from its Chief Risk Officer entitled FDIC's Supervision of First Republic Bank. The FDIC was First Republic Bank's primary federal banking agency, as First Republic was a state-nonmember bank. The report is basically a post-mortem of the FDIC's supervision of First Republic leading up until its failure in May.

The FDIC's report stated that the "primary cause of First Republic's failure was a loss of market and depositor confidence, resulting in a bank run following the failure of Silicon Valley Bank (SVB) and Signature Bank on March 10 and 12, 2023, respectively." As we noted in May, a unique feature of these post-mortem reports is that they include a great deal of supervisory material that is usually not public and closely guarded as confidential supervisory information. The FDIC's report went on to state that until April of 2023, First Republic had been well-rated with the highest two ratings for all components in its CAMELS exam reports. The FDIC went on to state that notwithstanding the generally well run nature of First Republic, "there were attributes of First Republic's business model and management strategies that made it more vulnerable to interest rate changes and the contagion that ensued following the failure of SVB." The FDIC noted three factors: (1) rapid growth and loan and funding concentrations; (2) overreliance on uninsured deposits and depositor loyalty; and (3) failure to sufficiently mitigate interest rate risk.

The FDIC's report concluded, even with the benefit of hindsight, it's unclear whether earlier supervisory action to criticize First Republic's interest rate or liquidity risk management would have prevented the failure given the speed of withdrawals following SVB's failure. However, it noted "meaningful action to mitigate interest rate risk and address funding concentrations would have made the bank more resilient and less vulnerable to the March 2023 contagion event."